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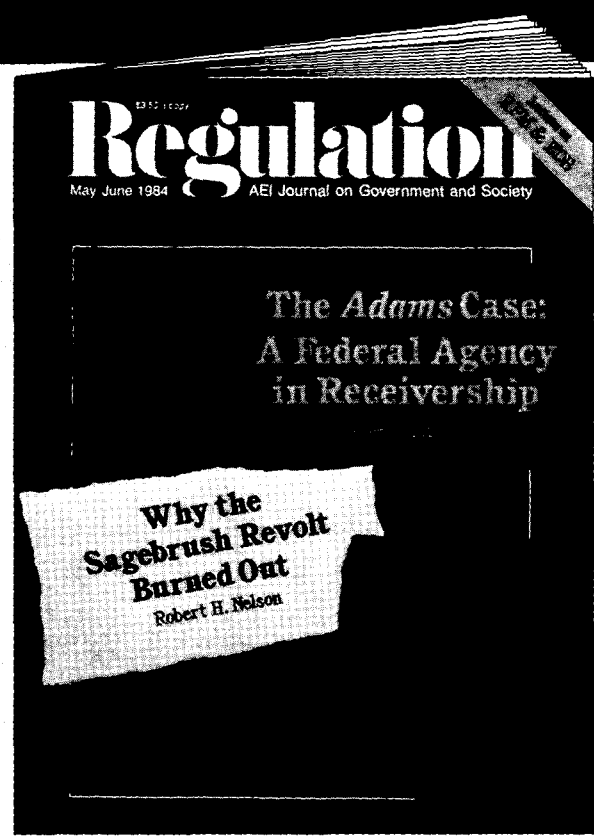

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Letters

We welcome letters from readers, particularly commentaries that reflect upon or take issue with material we have published. The writer's name, affiliation, address, and telephone number should be included. Because of space limitations, letters are subject to abridgment.

Preparing for the Next Oil Shock

TO THE EDITOR:

Huzzahs for "The *Next* Oil Shock: Giving the Market a Chance" (*Regulation*, March/April 1984). While George Horwich and David Weimer perform a real service in confusion reduction, they unfortunately sow some confusion of their own on several smaller but important issues.

(1) The authors call for monetary ease to "offset the drag and . . . facilitate the movement of resources" during an oil disruption. A disruption causes a real shift in relative prices that makes it socially efficient for resources to shift among sectors; some short-run unemployment of resources during this shift is a socially productive investment in the search process, yielding greater productivity later on. Monetary ease, which merely expands the *nominal* quantity of money, cannot undo this real relative price shift, and therefore cannot in any long-term sense offset the drag. Inflation will offset the drag in a short-run, illusory sense by creating an illusory increase in (nominal) demand in all sectors, thus delaying the inevitable reallocation process. And since inflation itself is a tax, affecting various sectors disproportionately, it will add its own "deadweight-loss drag" to the "oil price drag." Government already has enough incentives to inflate; let us not provide it with an excuse.

(2) The authors are right to point out that the oil-sharing agreement of the International Energy Agency (IEA) cannot do much good directly. In fact, it is unlikely to have much direct effect of any sort, since international price controls could not be enforced. It is also conceivable that IEA sharing could serve as an excuse for import quotas, although few governments would be anxious to drive up domestic oil prices even further during a disruption.

But the silver lining of the IEA agreement is that it implicitly precludes *export* controls during disruptions. Governments would be much more tempted to proscribe oil exports than imports during a disruption. Thus its net effect might be unexpectedly beneficial, so long as market prices are charged for any transfers that take place.

(3) There is no need to counter embargoes directed against one country, because they have utterly no effectiveness under any conditions. Oil can be reallocated easily, as it was in 1973 during the embargo against the United States and the Netherlands. It is dangerous to hold foreign and other policies hostage to an empty embargo threat, and it is high time that the public be told that it has one less thing to worry about.

(4) It is somewhat misleading to lump together the Carter and Reagan efforts to fill the Strategic Petroleum Reserve (SPR). The Reagan administration can take credit for about three-quarters of the more than 400 million barrels now in place. More to the point, there is nothing graven in stone about the many (poor) benefit-cost studies to which the authors refer for support of their SPR goal of 750 million to 1 billion barrels. It is far from obvious that we should rush to fill a large SPR at a time when oil prices are falling, real interest rates are high, Mideast oil is diminishing in importance, future disruptions are likely to affect prices less than past ones, and there is substantial excess production capacity.

(5) What exactly is the authors' basis for asserting that the SPR has no natural political constituency? Plenty of special interests favor distribution of SPR oil at below-market prices as another way to get their hands on "cheap" oil during disruptions. After all, why is it that the same people arguing for controls argue also for a faster SPR fill rate? And part of the oil industry would prefer for the government to confiscate the taxpayers' oil rather than its own. We have thus the makings of an interesting political coalition.

(6) The authors argue, incorrectly, that the social benefit of SPR crude oil exceeds its market price. That assertion is inconsistent with the later proposal that an import fee be used for SPR financing purposes. For if society at large is the main beneficiary, then society at large ought to bear the investment cost. More to the point, the industry does pay for the SPR oil when it buys it at market prices during future disruptions. The import fee proposal amounts to an argument that the industry pay for the SPR twice. The taxpayers invest in an SPR because the market expects controls (i.e., confiscation) and so invests too little. Since SPR sales revenues would belong to the taxpayers, it is appropriate that the taxpayers make the initial investment, particularly since this (risky) investment is a penalty for the voters' (implicit) past sins: the controls of the 1970s.

(7) Nor would earmarking the import fee for the SPR necessarily improve the incentives of the Office of Management and Budget. The earmarked fee revenue would simply replace the general revenue that is now used to pay for SPR purchases. The net effect would be simply to add the fee revenue to the general revenue fund. If a disruption occurs after the SPR is filled and the fees have reverted to the treasury, OMB will not relish the decision of which other programs to cut (during a recession) in order to refill the SPR.

(8) Horwich and Weimer's import fee is supposed to make up the purported difference between the market price and the social cost of imported oil. Since when does the government maximize social welfare instead of tax revenue? And what is the magnitude of the private sector inefficiencies caused by the tariff? Should we impose a tariff on bananas because increases in the demand for bananas drive up their price? If the answer is that the fee would transfer wealth to the "domestic economy," the response is that the fee makes the government better off and the private sector worse off.

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Even more puzzling is the argument that further benefits of the import fee include greater domestic oil production and revenue from the windfall profits tax. Benefits to the government are not necessarily benefits to society, and in a world of resource scarcity, more domestic oil production means less of something else.

(9) An SPR option system may substitute public for private stocks, resulting in little or even no increase in the total social stockpile. Moreover, I do not understand the authors' distinction between a political drawdown decision and an "economic" drawdown decision coupled with a political decision on how fast to refill. As long as the marginal choices are those of the government, the drawdown decision is in effect political.

(10) The appropriate goal of policy is efficiency in resource allocation, not maximization of SPR sales revenue. And yet incentives would be for the latter if, as the authors suggest, SPR revenues were earmarked for particular constituencies. Since these constituencies would receive SPR revenues but not bear the costs, the political system would be driven toward an ever-bigger SPR, to be sold at revenue-maximizing rather than welfare-maximizing prices.

Benjamin Zycher,
Jet Propulsion Laboratory,
California Institute of Technology

TO THE EDITOR:

I applaud the authors' view that "an essentially free-market response to an oil supply disruption is likely to prevail *only* if it is preceded by substantial government preparations." They rightly note that once a disruption has begun, "the only steps the government can take to reduce the costs are those that have been planned ahead of time."

The oil industry recognizes this fact, individual states recognize it, the International Energy Agency and its member countries recognize it, and Congress recognizes it. Unfortunately, the Reagan administration and the Department of Energy do not. I only wish Horwich could press his views more forcefully at the Department of Energy, where he now is a special assistant for contingency planning.

To date, the Department of Energy has failed to develop any specific plans to do any of the following in the event of an oil cut-off: (1) assist citizens unable to cope with oil price increases; (2) begin a public information program to help calm and inform a nervous and panic-prone public during a crisis; (3) begin a "fair sharing" program to ensure that oil companies who volunteer supplies to meet our international obligations will share the burden equitably (many, if not most, companies have very rightly said they will not participate in such a program without fair sharing); (4) meet our international oil-sharing obligations if voluntary U.S. oil company offers prove insufficient; and (5) allocate some portion of the Strategic Petroleum Reserve (through "directed sales") to help meet special needs, including state and local needs for emergency services and so forth. Most of these issues can be addressed now administratively by the department, rather than through legislative action. To underscore the bipartisan nature of these concerns, I might add that when the House Committee on Government Operations recently issued a report highly critical of the administration's failure to address these issues, not a single dissenting opinion was attached.

I am convinced that if the administration remains as ill-prepared as it is today, Congress will surely step in and act for it in the event of a crisis. As the authors predict, Congress would likely resort again to price and allocation controls, despite every effort by those of us who remember what disastrous results they produced during the 1979 oil disruption.

Horwich and Weimer suggest directing revenues from SPR sales to the states in a crisis. It was intended, of course, for these revenues to be retained and used to replenish the reserve after an oil crisis has ended. But since the Energy Department has shown an unwarranted concern over depleting the Treasury in order to fund an emergency economic response program, the authors' suggestion to use the incoming SPR revenues may well be one of the few avenues—if not the only one—by which the administration would agree to implement such a program. Accordingly, the suggestion deserves further consideration by both the administration and Congress.

On the authors' call for an SPR options program, I should note that the Chicago Board of Trade expressed some reservations about SPR futures in response to a query from the Energy Department. Among other things, the board suggested that it might not be possible to trade SPR futures contracts, since reserve oil for the most part consists of not one specific crude but rather a mix of several crudes. These concerns should be addressed. The House Energy and Commerce Committee, on which I serve, is about to take up a bill that would direct DOE to study an SPR options program and a "barter" program, as well as to conduct a limited test sale of SPR oil.

I agree with the authors' call for a 1-billion barrel SPR: for one reason, the larger our reserve, the more flexibility we have as to when and how to use it. As the authors note, the SPR budget has been far too subject to political and budgetary whim (primarily because of its size). For three consecutive years it has gone under the knife of OMB Director Dave Stockman, although Congress fortunately restored most of the proposed cuts.

Clearly, this national security program needs further insulation from the penny-wise but pound-foolish budget-cutters. I doubt, however, that an import fee is the answer, for both equitable and political reasons. Such a fee would hit one particular region of the country (the Northeast) unusually hard, and that area happens to have a sizable number of representatives in Congress, among them the Speaker of the House. And some of us true believers think that keeping oil prices artificially high, as an import fee would do, is a crime almost as heinous as holding prices artificially low.

Horwich and Weimer have presented a solid case for the absolute necessity of preparing now for a possible oil crisis. But I suspect they need to convince the Department of Energy more than your readers.

Mike Synar,
2nd District, Oklahoma,
U.S. House of Representatives

TO THE EDITOR:

Horwich and Weimer join the broad consensus of economists on oil supply disruptions. That this consensus extends across a wide political spectrum is evident from recent books produced by Resources for the Future and the Harvard Energy Security Program. As a subscriber to the consensus I applaud its promotion. As a pragmatist, however, I suspect that Horwich and Weimer

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have merely added their voices to ours shouting into the wind.

Aside from academics and the Department of Energy, not many want to give the market a chance. A bill to reinstate the ill-conceived regulations of the 1970s passed the Senate 85-7 in 1982. It behooves those of us who advocate market policies to reflect on the reasons why they inspire so little faith even in the private sector. It is unfortunate that the authors have not done so.

A likely explanation is that the market does not in fact work very well in the *short* run. There is little quarrel that, given enough time, the market will adjust to balance supply and demand. But the very term "shock" suggests a short time horizon, in which it is far from obvious that the adjustment would be smooth or efficient. In their article and in the book on which it is based, the authors merely *assume* that the market works well: it is hardly surprising that their arguments fail to persuade those not already converted to the free-market faith.

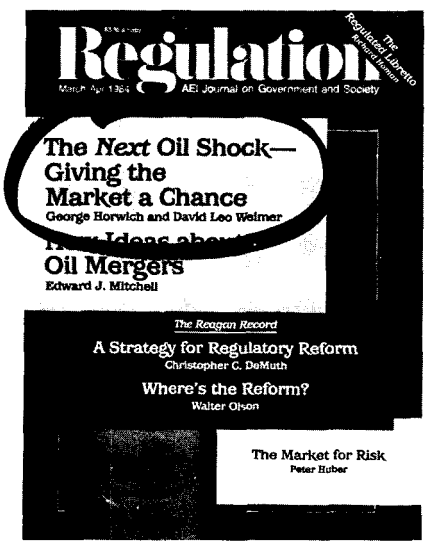
The question of how well the market works is not easy to answer definitively, but some suggestive evidence is provided by contract prices. In the authors' frictionless market, any difference between the price of oil bought under contract and the price of oil bought in the spot market would be arbitraged away immediately. In fact, spot and contract prices diverged by large amounts, for an extended period of time, during the Iranian crisis. A single "market price" simply does not exist.

Further evidence comes from the buy-sell regulations, which forced sales from large to small refiners at average, rather than marginal, cost. Although the authors properly condemn this program as unfair and inefficient, close examination shows that forced trades occurred even in periods when average and marginal cost were roughly equal, suggesting that small refiners did not have access to crude oil at the "market price."

Discussions with oil company executives leave me with the impression that existing contracts, whether explicit or implicit ("good business practice"), will prevent easy reallocation of large volumes of oil in a short time. Many think government intervention inevitable, and some even desire it on the grounds that emergency response is a public-sector responsibility.

Most of the authors' policy recommendations would be beneficial even if their premises proved to be wrong. Admitting that the market just *might* not work perfectly, however, raises the possibility of a more activist public policy. The trick is to design such policy so as to be helpful if the market does not work well, and do no harm if it does. One example is to improve the international oil-sharing mechanism, rather than scrap it as the authors suggest. Another is to restrict some of the auctions of Strategic Petroleum Reserve options to small refiners, who should bid the price up to market-clearing levels anyway.

The alternative to a little government intervention is not the pristine picture painted by the authors,



but the ham-handed regulation of the 1970s. Let us not forget that the first energy czar, the man who set up the regulations and made them work, was that leading advocate of free enterprise, former Treasury Secretary William Simon.

Robert Weiner,
Harvard Energy and
Environmental Policy Center

TO THE EDITOR:

The Strategic Petroleum Reserve has already been filled to a level of something close to a 100-day supply of current imports—without any help from oil import fees. And if an oil-import fee is enacted, it will be hard to remove once the SPR is filled. In fact, the authors openly propose having the revenues from the fee revert to the general fund at that point. Companies that depend on imports would probably petition Congress for a new entitlement program of transfers from companies with domestic supplies. Finally, oil exporters are not likely to stand by idly without retaliating while the U.S. government attempts to siphon off some of their revenues.

We do not believe that the authors' scheme of emergency subsidies to states, affected businesses, and consumers can be made to work in a manner consistent with the free market. We see no gain in embracing such redistribution (and, incidentally, spawning constituent groups intent on preserving the program) in order to prevent oil price controls. The two ideas are equally undesirable.

We do agree with the authors that it might be worth exploring a market mechanism rather than relying on the political system to signal the need to draw down the SPR. There are potential problems, however, with the authors' suggested options method. We believe it would be difficult to set the strike price of the option before an oil interruption occurred. Further, we are concerned that should oil prices rise in a disruption to a point where the option becomes highly profitable, the federal government might try to recapture the resulting "windfall profit."

While the auction concept presents difficulties, two other ideas come to mind. The first is to sell options to purchase SPR crude at whatever market price prevails during the disruption. The purchasers would be paying for assured access to SPR crude, without any price guarantees. The value of this "insurance premium" would of course vary from one oil user to another. A refiner that perceived that its sources of crude were at higher risk than its competition's might be quite willing to pay a fee to ensure access to crude.

The other possibility that should be considered is to hold ongoing sales of crude from the SPR at a fixed premium over generally available domestic crudes. This premium could be set at some level, say 50 cents to a dollar per barrel, that would give purchasers no incentive to buy SPR crude in normal times. If SPR sales begin rising, it would be a signal that oil markets were forecasting a diminution of total U.S. supply and were paying a premium for security. If sales reached a certain volume, say a half million barrels/day, it would trigger the currently planned auction system

(Continues on page 35)

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Perspectives
on current developments

Revision without Revolution in Carcinogen Policy

On May 22, 1984, the Office of Science and Technology Policy released a sixty-seven-page draft of a report intended as a "framework for regulatory agencies in assessing cancer risks from chemicals." After public comments come in, a final version is to be published this fall. The draft emphasizes that it is intended not to "formulate policy" but to "articulate a view of carcinogenesis that scientists generally hold in common" and to "clearly distinguish" between "statements of what is generally accepted as fact" and "judgmental (science policy) decisions on unresolved issues."

No one can fault an effort to lay out clearly for regulators what scientists know about carcinogens. And this report presents a much less tendentious and more balanced discussion of the disputed scientific issues than the carcinogen policy unveiled by the Occupational Safety and Health Administration in 1980 (discussed in these pages, March/April 1980).

One topic will serve for all as manifesting this improvement, namely, the vexed question of the use of massive doses in animal cancer testing. The OSHA policy recognized no such thing as an overdose. That is, it considered substances to be carcinogens if they led to an increase in tumors at any dose level, including one where toxic effects were unmistakably evident. Moreover, it specifically ruled out the possibility that such a verdict could be legally challenged on the ground that overdose-related side effects (such as the debilitated health of the animals) might have raised the tumor incidence. The new paper, by contrast, recognizes this possibility:

> [H]igh doses may themselves produce altered physiologic conditions which can qualitatively affect the induction of malignant tumors. Normal physiology, homeostasis and detoxification or repair mechanisms may be overwhelmed and cancer, which otherwise might not have occurred, is induced or promoted. [If so,] a toxic response at [the highest] dose may not be indicative of effects at low exposure levels.

OSTP's report still favors using test doses far above human exposure levels in order to overcome the "inherent insensitivity" of animal tests. However, it specifically endorses setting maximum dose levels in the light of pharmacological data to guard against disproportionate build-ups of the chemical or its metabolites within the test animal. That is to say, a serious effort should be made not to induce cancer by overloading or poisoning the mice. Long-suffering regulatory critics will find these words as refreshing as a cooling stream after a long trek through the desert.

Still, a close reading of the new document reveals that it has not succeeded in its professed goal of distinguishing science from "science policy." Instead, it contains instance after instance where policy masquerades as science.

Consider three examples. The first is the question that underlies all use of animal tests in regulation, namely, how well do animal tests predict human risk? One would have hoped for a thorough review of the record of animal tests in making valid human predictions. The report's discussion of this crucial question, however, largely consists of the following assertion: "But a finding of carcinogenicity in rodents is proof that the chemical is carcinogenic in a mammalian species. This must be taken as strong evidence that the chemical can be a carcinogen in man. . . ." Thus, instead of proving that animal tests are good predictors, the paper simply gives its rationale for assuming that they are. Elsewhere, the paper informs us that "this principle has been accepted by all health and regulatory agencies"—which begs the question entirely, since the point of the pa-

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per is to establish government-wide principles and, where necessary, to change principles that were accepted by agencies as a policy, not scientific, decision.

What *is* the scientific evidence on this point? It is thin, and hence can be summarized briefly. Hundreds of chemicals have by now been found to be carcinogens in animal tests, but epidemiological evidence in humans is available for only a fraction of them. Only a small number of these—somewhere between ten and twenty (depending on which authority one reads)—are also positive in humans. Thus, among the hundreds of animal carcinogens, fewer than two dozen have been confirmed to be human carcinogens as well. That is not a very large sample on which to base a generalization.

Of more importance is the question whether there are any confirmed cases where positive animal findings have *falsely* predicted human cancer risk. There are not. But this is a trivial consequence of the fact that there is no way to discover such cases even if they exist. The reason is that human epidemiology studies are statistically too insensitive to distinguish a substance that is not a human carcinogen at all from one that is merely quite weak, causing only one cancer in 10,000 subjects or one in 1 million. Thus, even though there are instances where the epidemiological evidence suggests that an animal carcinogen is not a human carcinogen—as in the cases of saccharin, DDT, and hair dyes—we cannot know this for sure.

How about negative animal results? Could one at least rely on thorough, well-conducted animal tests to establish that a substance does not cause cancer? Even this type of prediction, as it happens, is soft. It is, to be sure, a staple of the regulatory defense of animal tests that, as the new report says, "known human carcinogens, with the single exception of arsenic, are carcinogenic in appropriately conducted studies in some animal system." That might make it sound as if false negatives in animal test results are rare. The catch is that the report is including in its generalization a multitude of animal test designs, some of which—such as skin painting, injection, or intrabronchial implantation—are not normally carried out for regulatory approvals. Were these nonstandard tests excluded, the false negative rate might be higher. Thus the truly useful questions the report could have asked are these: How many false negatives are there if the only evidence available is that of standard test designs of the type and on the species of animals generally used for regulatory purposes? And can a chemical that comes out negative in those tests be considered safe for humans? The new report, unfortunately, is absolutely silent about these important questions, even though they, unlike the question of false positives, can in principle be answered on the basis of currently available data.

Thus, with regard to both positive and negative outcomes, the belief among regulatory agencies that animal tests predict well for humans is based on policy judgments, not strictly scientific ones. OSTP's new report is remiss in not making this explicit and in not discussing the evidence, such as it is, that supports this belief.

Policy can also be discerned to be cloaking itself in science in some of the report's recommendations on how animal tests should be designed and interpreted. Early on, the report expresses a pious wish that guidelines for long-term tests "should be designed to achieve an appropriate balance between the two essential characteristics of a biological assay: [a]dequate . . . sensitivity (a low false negative rate) and adequate . . . specificity (a low false positive rate)." Unfortunately, that praiseworthy intention cannot be carried out with respect to human cancer prediction. Regulators cannot alter their animal testing techniques to lower the frequency of erroneous predictions of risk to humans because, as discussed above, one cannot identify when those predictions are wrong. Instead, regulators (and the new report) fill the void of scientific knowledge with a policy value—that of "prudence." The most "prudent" course, naturally, is the one most likely to yield a positive outcome, and thus avoid false negative errors. This amounts to the principle of banning ten innocent chemicals rather than letting a guilty one go free.

Such prudence is rather different from achieving an "appropriate balance" between false negatives and positives, but this policy choice nonetheless underlies many of the report's recommendations. For instance, the report suggests that benign tumors should often be counted in with malignant ones for statistical analysis, which means that benign tumors can supply the margin of difference in de-

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termining whether a substance is judged a carcinogen. It also recommends calling a substance a carcinogen even if it does not raise the incidence of tumors but merely speeds up the appearance of spontaneous tumors that would have arisen anyway. The report explicitly endorses defining the term carcinogen "in a broad sense" in an effort to be prudent.

The problem with this is that the central issue in regulatory decision making lies in deciding which risks matter; the report never discusses what happens when the strong signals of powerful carcinogens are lumped in with and swamped by all sorts of weak and feeble effects. Thus the decision to treat carcinogens "in a broad sense" is likely to undercut the effort to treat them in a serious sense.

Policy is also smuggled into the report's discussion of a third area—the controversy over whether there is a threshold dose level below which a chemical has no carcinogenic effects. The report rejects thresholds and endorses the Delaney "no safe dose" approach to low doses. It cites the differences in individual sensitivity among a human population of normal genetic diversity, arguing that one could never rule out the possibility that someone, somewhere, might be sensitive to any exposure, however low. Also, given the limited size of animal tests, some rare adverse effects might always go undetected. Finally, the report notes the possibility that one carcinogen might interact with others to produce cancer even when consumed at a level that, when tested alone, produces no evident effect. For these reasons, no truly safe threshold dose for an entire population could ever be demonstrated experimentally.

These considerations sound like scientific ones, but they conceal a prior policy judgment. Why? Because only carcinogens are treated in this way: ordinary toxins (such as table salt) have long been regulated on the basis of pragmatically established "safe" dose levels, below which the risk to the public is believed to be insignificant. These are determined by first identifying "no observed effect levels" on the basis of routine animal tests and then adding a safety factor for extrapolating to humans. Clearly this method of setting levels cannot prove that the risk to the public is perfectly zero; rare sensitivities and interactions could always occur. Also, there are no obvious differences between carcinogens and toxins in the shape of experimentally observed dose-response curves. Both typically look "threshold-like"; that is, they show upward curvature at high dose levels and are, as scientists put it, consistent with being flat at sufficiently low doses.

Why, then, treat carcinogens so very differently from toxins by insisting on a "no safe dose" policy? The main argument given runs as follows. If a carcinogen is of the type that acts by damaging the DNA of body cells, there is some probability, however small, that a single molecule of it will induce a cancerous cell that could eventually grow to kill the host. Single molecules of toxins, on the other hand, cannot kill. But this distinction is seriously muddled precisely by the policy of defining the term carcinogen "in a broad sense," that is to include substances that merely shorten latency, induce benign tumors, or "promote" already existing tumors. These substances do not necessarily act at the DNA level; as the report observes, certain benign tumors do not result from any heritable, irreversible genetic change and are fully reversible after their stimulus is removed. Nor is there the slightest reason for thinking that single molecules of mere "promoters" or "latency shorteners" are capable of producing cancer; they behave much more like ordinary toxins, which are satisfactorily regulated on the basis of threshold assumptions.

Despite some modifications, then, the main lines of thinking on the cancer issue remain much the same under the Reagan administration as under its predecessors. The report's view of carcinogenic risk mixes science and policy, and seems to be based less on a scientific attempt to gauge the likeliest actual level of risk than on a political desire to be "prudent" by adopting worst-case estimates.

Truth-in-Hospitalization

Should the public have legal access to data on the track records of its local hospitals? That is the hub of a controversy now raging at the Department of Health and Human Services. On April 16, 1984, HHS proposed new regulations that would require Peer Review Organizations (PROs) to disclose extensive data on individual hospitals on such sensitive matters as how often each hospital conducts a type of operation,

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how many patients survive those operations, how long those patients remain in the hospital, and what the hospital charges for its services. HHS also requested public comments on whether to allow disclosure of the track records of individual *physicians* as well—although it said it views the argument for confidentiality as more compelling in that case than in the case of hospitals.

Congress created the predecessor of the PRO program in 1972. PROs are review bodies selected by and under contract to HHS and run by local doctors. Their main function is to review the services financed by Medicare (and, at the states' option, Medicaid). The purpose is to determine whether hospitals' and doctors' services are medically necessary and of acceptable professional quality. Under the program, HHS selects a PRO for each state by competitive bidding.

To conduct their review, PROs gather information from patient records and from records processed by claims payers such as Blue Cross. Using this information, the review bodies come up with profiles of hospitals, accounting for patient diagnosis, length of stay, services rendered, discharge status of patients, and readmission rates. PROs also compile physician profiles and general indicators of hospital quality such as infection rates. The PRO can then take action against providers that it believes have rendered unnecessary or low-quality service. Major employer groups, which are also seeking to control health costs, are likewise contracting with PROs for similar data, in hopes of steering employees toward the more efficient providers while ensuring that the quality of care does not suffer as costs are held down.

Individual patients who want to find out these things, however, remain somewhat in the dark. They can try to obtain information from PROs, but are often unsuccessful. Some PROs do not want to release information for fear of endangering the cooperation of hospitals and doctors in the peer review process. The proposed regulations would clarify and enforce an existing policy that requires PROs to disclose some data on individual hospitals to the public.

Disclosure advocates, who include consumer groups and employer groups, argue that such information could make a real difference for patients who now rely on at best anecdotal information before scheduling, for example, major surgery. Researchers have shown that hospitals that perform a lot of open heart surgery have a higher success rate than those that seldom perform it. They also maintain that disseminating information would strengthen competition on the basis of quality by intensifying oversight by payers and recipients of care and peer pressure from other health care providers —for example, pressure by doctors on the hospitals with which they affiliate. In New England, after studies were released showing tremendous variations in per capita rates of elective surgery, hospitals developed review procedures that resulted in significant reductions in the rate of elective surgery, reducing the cost and risk to patients of unnecessary surgery.

Several states, including Maryland and New York, have already been making some information available to patients since the mid-1970s. The public users have been primarily researchers and health planners, although the Health Research Group, a Nader organization, has assembled a consumer guide on Maryland hospitals' mortality rates associated with given procedures.

Hospital and doctor groups view the proposed disclosures as gross intrusions into the confidentiality of medical practice. They point out that hospital statistics can be seriously misleading. Hospitals that operate burn centers, for example, are likely to report higher infection rates. Likewise, a hospital that begins a program to take in emergency patients by helicopter may find its mortality rate climbing as it takes in more serious cases. Mortality rates for particular diagnoses may even double.

Raw statistics on physician track records would also be likely to mislead. A surgeon may be saddled with a high mortality rate simply from specializing in patients with complications. Moreover, even the best medical decisions are no guarantor of a good outcome.

If patients should start to scrutinize these indices, physicians might tend to work more and more "by the book," with little variation from the peer norm, in almost every aspect of medical practice from diagnosis to therapy. Standardization could replace the kind of experimentation that leads to medical advancement. Some physicians and hospitals may shun high-risk patients for fear of skewing their averages, or even refuse to perform the riskiest procedures altogether.

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Disclosure proponents are confident that these difficulties can be avoided by adjusting the raw statistics to sift out the variable factors and indicate the relevant quality differences. They note that such techniques of adjustment can be sharpened using Medicare's new basis for hospital reimbursement ("diagnosis-related groups") which attempts to account for variations in patient health status and other variables. Whatever the eventual sophistication of such techniques, however, they are still in their infancy—which does not help HHS much in its immediate regulatory decision.

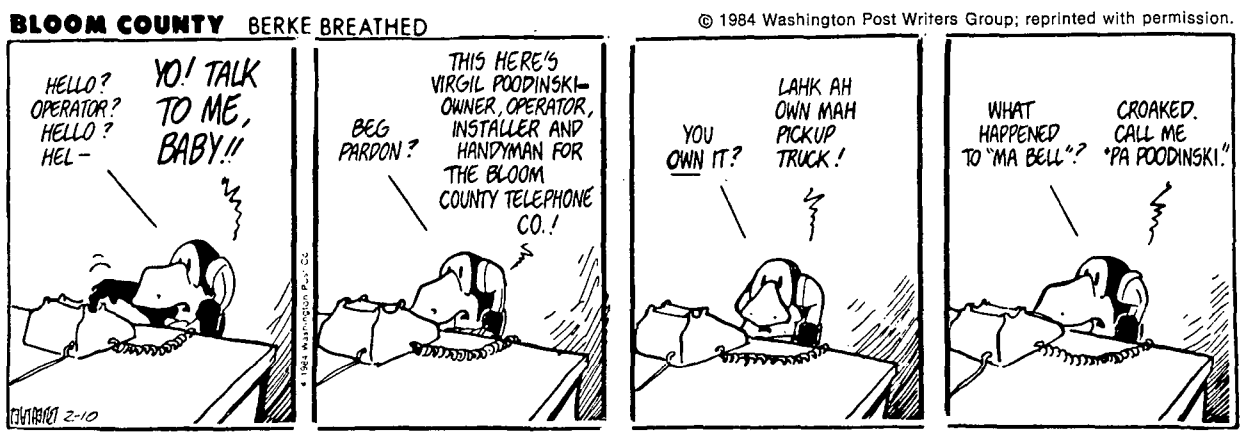
Sorry, Wrong Company? Competition in Pay Phones

Competition is coming to one of the humbler corners of the telecommunications network—the common coin-operated public phone. The $1.2 billion-a-year market for pay phones has always been a legal monopoly of local phone companies. That is now changing. In the latest of a series of deregulatory moves, the Federal Communications Commission voted on June 15 to allow private parties the option of installing their own pay phones rather than renting from the local telephone company. In the same month, anticipating the FCC action, Minnesota became the first state to give businesses (though not individuals) this option.

Contrary to what you might expect, pay phone competition is not just another by-product of the AT&T breakup. It owes as much to advances in telephone technology as to the trend toward deregulation. Until recently the only type of coin telephones available depended on the phone company's resources in several ways. Pay callers could speak to an operator at the telephone company's central office. Special equipment in the central office conducted electrical exchanges with the phone terminal to verify initial coin deposits, ring little chimes to signify that a coin had been inserted, return the coins after a busy signal or no answer, and trigger messages announcing rates and charges to the telephone user. Coin phones also depended on special metered lines to tell how long a call was taking. When the FCC decided back in 1975 to let customers hook up their own free-standing telecommunications equipment into the nationwide network, it did not include coin phones among the permissible equipment, since they were not free-standing.

Now, however, computer technology has created "smart" pay phones. These phones can perform all the same functions as the conventional pay phone, but using conventional telephone lines, and without contact with a central office or the assistance of an operator. These telephones are also self-contained: all the circuitry required to accept the coin, time the call, and so forth is contained in the telephone itself. Several manufacturers of such phones have sprung up in the past couple of years. The new FCC order essentially permits individuals and businesses to connect these self-contained phones to regular telephone circuits for interstate calling.

Local phone companies mostly opposed deregulation. Needless to say, they did not want to lose their monopoly, and warned that they might have to raise other rates to make up the lost revenues from coin service. But they also charged that some private owners might choose to buy antisocial telephone designs: phones


BLOOM COUNTY BERKE BREATHED
© 1984 Washington Post Writers Group; reprinted with permission.
HELLO? OPERATOR? HELLO? HEL-
YO! TALK TO ME, BABY!!
BEG PARDON?
THIS HERE'S VIRGIL POODINSKI— OWNER, OPERATOR, INSTALLER AND HANDYMAN FOR THE BLOOM COUNTY TELEPHONE CO.!
YOU OWN IT?
LAHK AH OWN MAH PICKUP TRUCK!
WHAT HAPPENED TO "MA BELL"?
CROAKED. CALL ME "PA POODINSKI."

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without the initial dial tone that grants coinless access to 911 emergency calling, or phones that do not accommodate the hard-of-hearing.

These concerns may have led the FCC to drop its initial plan, which was to preempt state regulation in order to ensure full deregulation of pay phones. Instead, it decided to let individual states come up with the rules, if any, and the rates under which these private pay phones will operate for use in local intrastate service. It is possible that some state might attempt to ban private pay phones by limiting their use with local service or by setting prohibitive rates, but the FCC could be expected at some point to override such attempts by declaring them inconsistent with the federal regulatory scheme. Thus some degree of nationwide deregulation is assured.

State regulators will soon have a lot of issues to settle. Local phone companies may seek to convince state regulators that they should receive some portion of the revenues that the private pay phones generate. That is what happened in Minnesota. The Minnesota commission requires businesses that buy their own coin phones to pay the telephone company $55.70 to $80.90 a month, depending on their locations, for the use of a special telephone line. They keep the revenue from the first 200 telephone calls a month and pay Northwestern Bell from five to ten cents per call thereafter, depending on the volume of calls. Assuming 300 calls a month at 25 cents apiece, that adds up to not much better than a break-even proposition—and of course the business is responsible for its own repairs. Still, this leaves businesses better off than they have been. In the past, Minnesota businesses that wanted a coin telephone had to pay the phone company for the privilege, at rates of between $32.90 and $76.10 a month per line, depending on their location. Moreover, they could not keep any of the revenue generated. (In some other states, the host business could keep a share of receipts.)

Another sticky issue for state public utility commissions will be whether to allow the prin-

"Then she began picking on the long-distance phone company I chose."

Drawing by Modell; © 1984 The New Yorker Magazine, Inc.

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ciple behind private pay phones—that firms should be allowed to "resell" local phone service—to spread further. Up to now telephone company tariffs have prohibited all businesses except for hotels, motels, and hospitals from reselling local service. On the other hand, resale of interstate long-distance service, which has been authorized federally, is now a big business.

Legalized resale at the state level may seriously cut into phone company revenues. Local phone companies provide much of their local service on a flat-rate basis, that is, not varying with usage. If firms are allowed to buy flat-rate service and resell the time on it to residential and business users, thus concentrating usage of the line, it will tend to become impossible to maintain the flat-rate fee. Minnesota resolved this issue by limiting resale to business lines that provide "measured" (metered) service. Other jurisdictions are likely to adopt the same approach, at least until residential metering becomes widespread.

A proliferation of private-party coin phones should have a number of effects. One is a great increase in the variety of phones. Phones might be specialized for calling across the city, across the state, or across the country, and could be structured to accept almost any credit card, not just the phone company's. Some would, others would not allow callers to talk to an operator. Another effect should be some degree of price competition, especially since local telephone companies can continue to erect both the old and the new type of pay phones on their own account. As pay phones become more numerous in stores and restaurants, however; they might become less numerous on the street —unless regulators decide to permit private pay phones in public areas such as airports and street corners.

Race, Ratchets, Redistricting, and the Voting Rights Act

By now everyone knows the story of how the original color-blind intentions of the civil rights acts were gradually turned into the color-conscious policies of busing, quotas, and affirmative action. Less well known—but illustrated in three cases pending before the Supreme Court—is the extent to which the purpose of the Voting Rights Act of 1965 has been transformed in much the same way.

Before the Voting Rights Act was passed, southern governments used a variety of procedural devices and pretexts to prevent black citizens from voting. (In one oft-told story, local officials gave black applicants a "literacy test" by handing them a Chinese newspaper to read.) These barriers began falling to court challenges in the 1950s and 1960s. As soon as one barrier was struck down, however, the local authorities could erect a different one—and there was an almost infinite variety for them to choose from. Polling places could be switched at the last minute. Applicants for registration could be required to obtain character references from already registered voters, nearly all of whom were white. The boundaries of whole cities could be gerrymandered to exclude those blacks who did manage to register. It looked as if southern governments might succeed indefinitely in keeping one step ahead of the courts —and keeping blacks out of the voting booths.

Congress responded to this problem with section 5, the "pre-clearance" provision of the Voting Rights Act. That section requires most southern governments (and a few other jurisdictions around the country) to obtain the approval of the Justice Department or a three-judge panel of the federal district court in Washington before making any change that affects election procedures. The local government must prove that the change "does not have the purpose and will not have the effect of denying or abridging the right to vote on account of race or color."

The provision seemed to work as intended, and southern blacks began registering in large numbers. But then the focus of voting rights cases began to shift away from the question of whether minorities were free to vote, and toward the question of whether their votes were being "diluted." This dilution could take many forms. For example, a city might dilute the clout of a growing minority population by annexing an all-white suburb. It could gerrymander its city council map to split up a minority neighborhood among several districts, or abolish districting entirely in favor of at-large elections.

The Supreme Court interpreted the act to prohibit any electoral change that caused "retrogression" in minority impact on govern-

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ing bodies. The Justice Department proceeded to approve such changes only when the local government agreed to take other steps to increase the likelihood that minorities would be elected to office. If a city wanted to annex a suburb, it might be required to drop its at-large system of city council elections.

This emphasis on combating dilution had several problematic consequences. In the first place, there were plenty of nonracial reasons why cities might annex suburbs, employ at-large voting systems, or adopt this or that redistricting scheme. Under the law's effects test, none of these reasons could be considered relevant. Second, the ban on retrogression created a ratchet whose eventual end-state was a goal Congress had never endorsed: proportional representation by race.

Finally, the penalty for a local government's nonconformity sometimes fell on the wrong party, namely the voters. When the Justice Department refused to approve a redistricting plan, the result was often to delay or even abolish the elections in question. Richmond, Virginia, saw its city council elections delayed for five years in this way. New York City delayed council elections by a year, and Georgia held up congressional elections by a month. The law not only wound up suspending the process of local democracy it was intended to protect, but even gave local officials a perverse incentive to remain intransigent.

Until quite recently, these problems were mostly confined to southern jurisdictions. The only way the Justice Department or private civil rights plaintiffs could change the structure of other local governments was by going to court and getting them declared unconstitutional. Such challenges were often attempted during the 1970s, even outside the South, but their success was spotty at best. Some courts found a disparate *effect* to be sufficient in cases of prolonged, complete exclusion of minorities from elective office. Others refused to step in without a showing of discriminatory *intent*.

The Supreme Court was given many opportunities to formulate a theory on vote dilution, but for years it remained coy. Only once, in the Texas case of *White* v. *Regester* (1973), did the Court strike down a scheme on grounds of illicit vote dilution. It did not, however, specify whether its objection hinged on discriminatory intent or disparate effect. Finally, in the 1980 case of *City of Mobile* v. *Bolden*, the Court began to clarify its position. A district court had ordered the city of Mobile, Alabama, to switch from a commission form of government, elected at-large, to a mayor-council form, with nine council members elected from wards drawn so as to provide approximately proportional representation for blacks. A plurality of four Supreme Court justices reversed the lower court decision on the ground that the plaintiffs had not proven discriminatory intent, which was the standard, they held, that applied under both the Constitution and section 2 of the Voting Rights Act. Two other justices concurred on different grounds.

Despite the split in the Court majority, it was clear enough that something close to a discriminatory intent standard was emerging. Civil rights advocates therefore turned to Congress, which was preparing to extend the preclearance provisions of the act, to overturn the *Mobile* decision, and to go much further. The House of Representatives passed a bill adding to section 2 of the act—a section applying to all local governments—language that, as the committee report made plain, was intended to incorporate the standard that the Justice Department had long used to force progress toward de facto proportional representation in the South.

This change extended the impact of the law immensely. It meant that the Justice Department could sue under its own expansive standard to overturn existing structures, not just new ones, throughout the entire nation, not just the South. It also meant that private parties could sue to overturn a plan under the more ambitious standard whether or not the department had approved it. In an eerie pre-echo of the later *Grove City* maneuvering, proponents billed the change as a minor technical correction of the Supreme Court's misinterpretation in the *Mobile* case.

The Reagan administration and some senators were convinced that the House bill went too far. The eventual result was a compromise among the Senate, House, and President. The compromise bill kept the provisions extending scrutiny to existing procedures nationwide, but revamped the standard of proof by codifying language from the Supreme Court's confused opinion in *White* v. *Regester*. The civil rights plaintiffs described this language as an effects

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test, and their critics in Congress as an intent test. The bill also provided that "nothing in this section establishes a right to have members of a protected class elected in numbers equal to their proportion in the population."

Ironically, the week that the compromise was signed into law, the Supreme Court clarified its earlier ruling to show that *White* v. *Regester* indeed incorporated an intent test (in a case in which it held that the plaintiffs had met that standard). This has not forestalled a wave of litigation under the new 1982 provisions. In perhaps the best-known case, Jesse Jackson has sued to overturn the system of runoff primaries used in many southern states; the voting rights section of Justice unsuccessfully asked its superiors to support him. Nor has it forestalled the lower courts from adopting an effects rather than an intent test, by relying on statements by civil rights advocates in Congress that they intended their codification of *White* v. *Regester* to be applied as an effects test, regardless of how the Supreme Court thereafter might explain its own decision.

The statutory disclaimer of proportional representation has also been thoroughly reasoned away by the courts, as congressional critics had warned. Judge John Minor Wisdom of the Fifth Circuit Court of Appeals has said in the 1984 case of *U.S.* v. *Marengo County Commission* that the disclaimer means only that the mere absence of elected minority officials is not *by itself* enough to trigger a violation of the act. Such an absence is ordinarily sufficient, however, he said, when combined with racially polarized voting. Since polarized voting unfortunately occurs in nearly every jurisdiction in the country—even where local officials try valiantly to discourage it—the absence of minority representation is indeed illegal.

Judge Wisdom indicates that a court may correct such an absence by imposing gerrymandered single-member districts or by other measures:

> Alternatively, all nine members could be elected at-large, but each voter could be given the right to vote for only five candidates, thus insuring that minority political interests have a chance to elect members of the board. Other alternatives are cumulative voting and transferable preferential voting.

These sorts of electoral systems are used in such countries as Ireland and Australia, and they have a name—proportional representation. It is exactly what Congress and the Justice Department have long purported to disclaim.

Three redistricting cases, from North Carolina, Mississippi, and Texas, are now before the Supreme Court on appeal. The North Carolina case illustrates one of the problems with the current state of the law, which is that the interests of minorities are not always monolithic. A number of blacks who had actually been elected to the state legislature sought to testify that the state's scheme of multi-member districts worked to the benefit of black voters. The lower court refused to accord any weight to their testimony, however, pointing out that the civil rights attorneys had already been certified as the sole legitimate spokesmen for the class of North Carolina black voters.

In the Mississippi case, the state legislature had come up with a plan to create two congressional districts with a black minority of 40 percent. The Justice Department disapproved this plan, and a federal court then created a district with a black majority of 53 percent. Too many blacks either stayed home or voted across racial lines, however, because the district elected a white candidate in 1982. The plaintiffs went back to court in 1983, and this time the court raised the black population in the district to 58 percent, which may be enough to do the trick.

Such decisions imply that where not enough members of a protected group choose to register or vote, or where division within the group enables members of the local minority to slip into office, the courts will pack enough members of the group into the district to make the result certain. The Seventh Circuit Court of Appeals has made this line of reasoning explicit in a case involving the Chicago city council (an example of the new nationwide scope of the act). The court found that minorities are entitled to districts in which they form "an effective majority," in the judge's words, which means "a majority of the population substantial enough to allow group choice to be effective." The court indicated that in some cases even 65 percent might not be enough.

Exactly the opposite result, however, was reached in the pending Texas case. The legisla-

(*Continues on page 38*)

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Slicing the Geostationary Pie

Property Rights in Orbit

Molly K. Macauley and Paul R. Portney

THERE MAY BE NO free lunch, but dessert is on the house at the Federal Communications Commission (FCC). For the second time in twelve months, the commission is about to give away a large number of shares of an outer-space resource that has become a mouth-watering delicacy to the telecommunications industry. But deciding who gets pieces of the pie is not easy. It requires the commission to assess and compare the technological sophistication, financial viability, and commitment to the "public interest" of all applicants—which, this time around, total twenty-one telecommunications providers and would-be providers. Nor is it really a "free" giveaway, even though users do not pay for the resource. In fact, the FCC's generosity may soon force every American business and household having a telephone, TV, radio, or computer modem to pay needlessly high rates for services.

If the FCC were willing to organize a market for this extraterrestrial resource, it could overcome both difficulties. A market would be much easier to administer than the current system of bureaucratic allocation and would ensure that the price of most communications services fairly reflects their costs. So far, however, the commissioners have yet to endorse the sale rather than the rationing of their wares.

Molly K. Macauley is a fellow and Paul R. Portney is a senior fellow at Resources for the Future, Washington, D.C.

The Pie in the Sky

The commission's five-star confection is the "geostationary arc," a precise orbit in space where most communications satellites prefer to locate. The arc is a tire-like ring positioned around the equator about 22,300 miles from earth (see diagram). When a satellite occupies such an orbit, its velocity not only perfectly offsets the earth's gravitational pull, but also exactly matches the twenty-four-hour rotation of the earth. The orbiting satellite thus appears from earth to be stationary. This in turn allows earth stations (the large transmitting and receiving "dishes" that dot the landscape) to aim their antennae only once, at the always-in-view geostationary satellite. Because of the curvature of the earth, a single satellite can keep only a portion of the earth's surface in view—which means that earth stations as far apart as Maine and Alaska, but not further, can communicate with each other.

A satellite in any other orbit, by contrast, is not always in the view of the same two sta-

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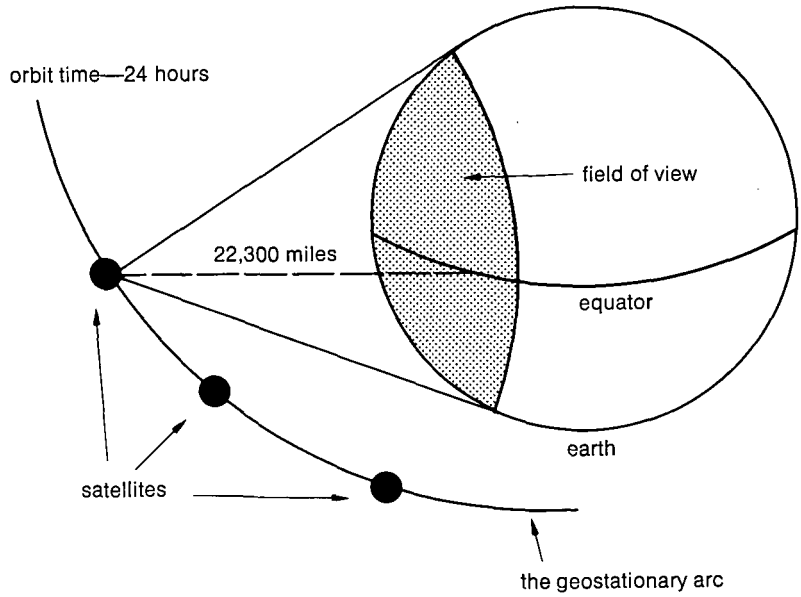

tions because it disappears below the horizon much of the time. In order to maintain continuous communications in this latter case, numerous satellites would be required (up to one hundred according to some estimates) along with complex earth stations having movable antennae that track the path of the satellites across the sky. Such a system would be extremely costly. Consequently, the most common alternative to geostationary satellites is terrestrial microwave facilities. For long-distance telephone communications, these consist of a network of transmitters, amplifiers, and relay stations spaced every 30 miles along the earth's surface. If the distances involved are greater than about 900 miles, using this sort of system for telephone transmission is more expensive than using a satellite in the arc. In fact, a nationwide long-distance telephone network using several geostationary satellites able to "see" the entire United States could save its owners as much as $500 million a year compared to a spider's web of terrestrial microwaves across the continent.

The usefulness of a slot in the geostationary arc is therefore obvious, and satellites occupying such slots are already providing us with a large and growing variety of services. Live television transmission via satellite began two decades ago, with the Tokyo summer Olympic games, and by now most live TV coverage is routinely beamed by satellite, as are popular cable network programs and radio broadcasts. Cloud-cover pictures on the evening news come from government-owned and -operated satellites located in the arc just off the east and west coasts. Moreover, 1985 will mark the twentieth anniversary of the use of satellites in telephony, a use likely to intensify given the vigorous competition developing in long-distance services. Finally, the arc is now home to satellites beaming newspaper copy and other text to regional printing offices. It is estimated that the services provided by satellites in the arc will gross as much as $10 billion in worldwide sales by 1990.

But the arc can accommodate only a finite number of satellites. At any given time, that number is limited both by current telecommunications technology and (as we shall see) by the mechanism the government uses to apportion them. Of the more than 200 satellites currently and soon to be stationed in the arc, about 60 percent will be parked in less than one-third of its length, along those parts either viewable by the United States or situated over the Atlantic Ocean so as to link the United States and Europe. Some seventy applications for slots above the United States (including ten renew-

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als) have been pending before the FCC since November 1983. Under present ground rules, these demands would more than exhaust the capacity of this part of the arc. With crowding becoming so serious a problem, the FCC opened a rulemaking six months ago to study and perhaps revise the ground rules and related policies.

Slicing the Pie

A hierarchy of authorities determines who gets which slices of the arc. First, the United Nations' International Telecommunications Union (ITU)—through global, regional, and even bilateral meetings—divvies up the worldwide arc. Since slots in the arc with a view of the United States are also ideal locations for both Canada and the nations of Central and South America, competition for them through the ITU is especially keen. As for U.S. use of the arc, the Commerce Department's National Telecommunications and Information Administration (NTIA) coordinates allocations for defense, weather, and other U.S. government purposes, while the FCC has the task of making allocations to U.S. domestic commercial users.

Actually, under current practice, the FCC must do more than just allot a fixed number of slots to applicants. It must also decide *how many* slots to allow in the stretch of the arc of interest to commercial users. This question arises because Mother Nature and the FCC's response to her whims impose constraints on the allowable spacing between satellites. For one thing, geostationary satellites tend to wander somewhat in their orbits due to solar and lunar perturbations. To reduce the chances of a collision, the FCC requires satellites to maintain a separation of one-tenth of a degree, or about forty-seven miles. That may be overly conservative. Even if satellites were spaced more closely, the chances of a collision would be infinitesimally small.

... the FCC must do more than just allot a fixed number of slots.... It must also decide how many slots to allow....

The binding constraint, however, is a second one—interference. If satellites were situated only 47 miles apart in the arc, they could not communicate at the same time on the same frequency without interfering with each other's signals. This interference problem might not be very serious if satellites could use many different frequencies, but the FCC has allocated only a small chunk of the frequency spectrum for satellite use (see *Regulation*, May/June 1983). Because of this frequency crowding, the FCC has had to rely on wide spacing. In August 1983, after it had been flooded with slot requests, the FCC cut its previous minimum spacing in half to 800 miles, where it stands today. By freeing up more spectrum for their use, the commission could reduce the spacing between satellites and thereby increase the number of arc slots.

Once it has decided on slot-widths, how then does the FCC choose among commercial applicants for these valuable pieces of galactic real estate? How does it decide between an application for expanded service from a well-established satellite company and one for unique services from an entrepreneurial newcomer? It does so in much the same way that it allocates the electromagnetic spectrum to conventional radio and TV broadcasters or that the Interstate Commerce Commission awards new routes to truckers: through an administrative process known as "allocation under a public interest standard." And as in the case of traditional trucking regulation, the competing applicants can file long briefs explaining why their rivals should not get the slots. The decision process customarily takes little heed of either the value of a slot to competitors or the economic benefits to consumers.

This creates a nightmarish regulatory dilemma. What criteria best measure the "public interest"? In a succession of rulings, the FCC has imposed a number of standards on applicants. These have ranged from requiring "prompt and efficient utilization of orbital locations," through prohibiting excess capacity and specifying particular technical requirements, to insisting that contestants for slots demonstrate "financial viability." No one doubts that these and other criteria have something to do with the public interest. Unfortunately, as in the case of transportation regulation, each criterion generates a different rank-

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ing of applicants. So the final selection from among competing applicants cannot but appear arbitrary.

A major problem is that the FCC's allocation procedure encourages firms to apply for slots merely on speculation they can use them.

A major problem is that the FCC's allocation procedure encourages firms to apply for slots merely on speculation they can use them. In both the 1983 and current rounds of slot allocations, the commission imposed a cut-off date for submitting slot applications—a practice that naturally tends to create a land-rush mentality among applicants. And since applicants pay nothing for a slot (save for the cost of preparing an application), they lose nothing if they receive one they fail to use. Consumers, of course, *do* lose if there are viable current uses for a claimed but unoccupied slot. At least one industry participant has expressed for the record what must be common talk in the locker room—that many of the seventy-odd applications are filed on behalf of systems that could never obtain sufficient financing to be built.

Consider how the FCC, faced with a deluge of applicants, goes about determining financial viability. As some applicants have pointed out, it is hard to secure firm financial commitments when prospects for success are unsure and subject to time-consuming deliberations at the FCC. Sympathetic to this bind, the FCC has in the past issued conditional satellite construction permits that give applicants a slot provided they adhere to a schedule on financing, construction, and so forth. However, monitoring applicants' progress step by step imposes added administrative costs on the FCC's already overburdened staff. And the process can also open up Pandora's box for traditional regulators at the FCC. In one recent case a conditional applicant, in a creative effort to secure financial commitments from an experienced incumbent in the arc, promised to swap some of its satellite capacity in exchange. Other firms in the industry promptly accused the conditional applicant of "trafficking" in permits—one of the worst sins in the regulatory syllabus.

Such entrepreneurship or, if you prefer, trafficking is a sure sign that a market is bubbling not far beneath the surface. It is worth spelling out what such a market in arc slots would imply.

How the Arc Could be Marketed

In this area of economic regulation, unlike many others, there is no question that government must play a basic role. If the government were to permit a market without first defining property rights in the arc and creating a mechanism to enforce them, it is unlikely that the arc would be allocated efficiently. Users could launch and operate new satellites without having to pay for their interference with other users (which would be a sort of pollution "externality"). Sooner or later, not only would there be too many users, but each of them would have reason to increase its transmission volume in an attempt to drown out its neighbors. Such an outcome could hardly be deemed efficient by any economic standard.

[The FCC] could auction off or rent out smaller units of arc . . . letting individual companies assemble as many degrees as they wished to form a slot.

After its initial definition of noninterfering slot boundaries, the FCC could ensure a vigorous market for subsequent arc use in one of two ways. It could either simply parcel out arc slots that would not interfere with each other and then sell or rent each of them to private users. Or it could auction off or rent out smaller units of arc, such as individual degrees, letting individual companies assemble as many degrees as they wished to form a slot. The alternatives are like those a developer faces in dividing and selling a large tract of land, where each subdeveloper must somehow be deterred from spoiling the land purchased by other subdevelopers (say, by blocking the view). The first solution is to "internalize" these undesirable effects—that is, sell indivisible tracts large enough so that nothing one owner does could possibly affect another. The second solution is

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to allow any configuration of purchases and to rely on special contracts or zoning rules to prevent negative spill-over effects. The FCC could implement the latter solution by technically defining a maximum level of interference allowable at the boundaries of any individual user's position of arc. Companies could then assemble slots of any size subject only to this rule.

These principles are hardly unusual. The government already limits commercial and other access to so-called common property resources such as underground aquifers and grazing lands, and it already collects revenues from the sale or lease of minerals, timber, and oil and gas (both offshore and on). If objections should arise as to the legitimacy of the government's claim to "own" the geostationary arc in the first place, initial arc slots could continue to be given for free as they are now or, for that matter, they could be distributed by lottery. The important point is that a secondary market be allowed to form so that present and prospective slot occupants would begin to confront the true opportunity costs of their actions. Such a market would, of course, be subject to the interference constraints discussed above.

An appropriately designed arc market would provide a number of other important advantages. Slots would tend to be allocated to their most efficient uses, since bids for sale and resale would reflect each firm's best-informed estimate of the consumer demand for its services. Such an approach would put to the real test—the market test—the financial viability of firms, and an ideal laboratory would be substituted for bureaucratic speculation. Creating a market could also end the land rush each time new slots go up for grabs, since new users could gain access (at a price) to the arc at any time. Incentives to stake out "free claims" would disappear.

Still more important are the benefits that would accrue over the longer haul. As noted, certain locations in the arc—especially those that have a full view of the United States—are much more desirable than others. Pricing would inevitably reflect the locational value of these sought-after slots, much as urban land values rise from block to block as one nears a downtown area. This would in turn spur innovation to take advantage of scarce locations. Just as the pressure of real estate prices gives rise to skyscrapers in terrestrial central business districts, so the most valuable arc slots might become home to multi-antennaed, high-capacity space telecommunications platforms designed to economize on arc. Some of these large platforms ("earthscrapers"!), designed to be arc-chintzy, are already on engineers' drawing boards. An arc market would hasten their development and manufacture.

Innovation in the mitigation of interference would also be encouraged. Just as the other inputs to signal reception have price tags—from the smoothness of the dish (surface imperfections cause "noise") to the sophistication of the electronics—so too should signal inaccuracy. The higher the rent for an arc slot, the more diligently designers would seek to eliminate noise. A company skilled in interference mitigation might find room to "squeeze" into a slot that was heretofore believed unusable because of potential interference. In fact, an arc market would also spur innovation in terrestrial technologies. The FCC's current practice of dispensing valuable arc locations free of charge has implicitly undercut innovation in fiber optics and terrestrial microwave communications systems, both of which must pay for their rights of way. An arc market would correct this inequity and stimulate innovation in earth-bound telecommunications.

The FCC's current practice of dispensing valuable arc locations free of charge has implicitly undercut innovation in fiber optics and terrestrial microwave communications systems....

What disadvantages might attend the creation of a market for arc? Perhaps the most daunting problem would be the transition from the current system of allocation. Existing satellite companies would hardly be eager to pay for what they now enjoy free of charge, and potential new entrants are geared up for administrative rationing rather than market bidding. Other regulatory areas, however, offer encouraging precedents for change. The airlines have had little trouble figuring out, and prospering from, experimental marketing of airport landing slots. Likewise, industrial firms caught on

(*Continues on page 51*)

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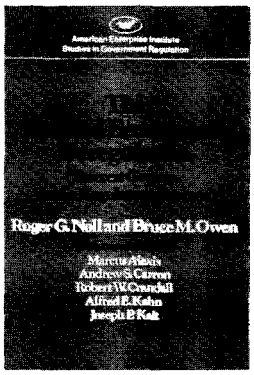

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The Subsidized Sagebrush: Why the Privatization Movement Failed

Robert H. Nelson

THE MOVEMENT TO SELL federal lands into private ownership arose somewhat later than the Sagebrush Revolt. Both movements posed a major challenge to federal land ownership, but from very different directions. The Sagebrush rebels stirred up considerable enthusiasm among a wide range of westerners, at least to begin with, but they never enlisted much intellectual support, perhaps because they had developed no consistent rationale for their crusade. Privatization, by contrast, was backed by a small group of intellectuals with respectable credentials who carefully developed their arguments in both scholarly and popular outlets. But they never attracted either interest-group backing or broad popular support.

Both movements foundered on the phenomenon of the Subsidized Sagebrush: the fact that the West has received major economic benefits from federal land ownership. In the end, "privatization" wound up having much less political impact than did the Sagebrush Rebellion.

Robert H. Nelson is an economist in the Office of Policy Analysis of the U.S. Department of the Interior, which does not necessarily agree with the views he expresses here.

This is the second of two articles in which he examines issues in public land management. The first, "Why the Sagebrush Revolt Burned Out," appeared in our May/June 1984 issue.

A Record of Inefficiency

Unlike the Sagebrush rebels, the privatizers argued from the beginning on grounds of economic efficiency and national well-being. Some of them saw privatization as a modest way for the government to rid itself of parcels that it did not need or could not easily manage. Others saw it more sweepingly, as a challenge to the root premise of government ownership itself. This group believed that public ownership and management inevitably led to such problems as the "capture" of federal land agencies by private parties and the use of clumsy command-and-control management techniques.

Both groups of privatization advocates could point to a large economic and environmental literature (parts of which overlap) on the failures of public land management. Economic studies have found that federal lands

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have long been mismanaged, resulting in shifts of public land from higher- to lower-value uses, investments in projects whose costs are much larger than their benefits, building at one site when another site would offer higher returns, consumption of resources when conservation would be more appropriate and, conversely, conservation when consumption would be more appropriate.

One much-studied example is the U.S. Forest Service. Reflecting a persistent lack of economic sophistication, the service tends to hold excessive inventories of timber, delay harvesting timber for too long, and misallocate investment funds. (See Thomas Lenard, "Wasting Our National Forests," *Regulation*, July/August 1981.) What is particularly disturbing is that the service harvests a good deal of uneconomic timber in prime recreational areas, thereby inflicting needless environmental as well as economic damage. In fact, John Baden and Richard Stroup have argued that the worst dangers to the environment may be those that occur when the government subsidizes activities that would otherwise be uneconomic, disrupting the functioning of markets and ecological systems at the same time.

. . . the worst dangers to the environment may be those that occur when the government subsidizes activities that would otherwise be uneconomic. . . .

The Bureau of Land Management (BLM) of the Interior Department has also been an inefficient manager of livestock grazing on public lands. Because ranchers have not enjoyed secure tenure on their grazing lands, they have often been unwilling to invest in improvements to the land. They might take steps to improve the growth of forage plants, for instance, but fear that the BLM might then allocate the resulting increase in the land's carrying capacity to wildlife instead of stock. This lack of investment incentive increases the pressure on the bureau to plan and finance improvements itself. Partly as a result, critics say, the bureau has managed to expand its staff and budget far out of proportion to the rangeland values at stake or the revenues it collects in grazing fees.

Both the BLM and the Forest Service operate their surface lands at a big loss. For example, it costs the BLM about four to five times more to manage grazing land than the land generates in revenues. Moreover, the Forest Service reports that its lands cost $1.8 billion to manage in 1980 and brought in total revenues of only $0.9 billion. The latter deficit is particularly striking given the nature of forest economics. One of the main expenses of ordinary forest owners is the cost of carrying capital—paying a mortgage or foregoing revenue while waiting for a stand of trees to grow to optimal harvest age. The Forest Service, however, pays no capital charges, and most of the timber it currently harvests comes from "old growth" forests on which it has never had to invest much money. According to Sterling Brubaker of Resources for the Future, "No one has ever established" that these discrepancies are matched by the value of environmental or other non-marketed outputs of the land. "In fact, it seems implausible for much of the land, which is without any special distinction."

Marion Clawson, widely regarded as the leading student of public land management, has concluded that the management record of the Forest Service is "unacceptable," perennially "rejecting economic considerations or economic analysis as applied to the national forests." The problem is not a matter of isolated willfulness, in Clawson's view, but an inherent defect arising from the service's status as a politically oriented body.

The pervasive inefficiencies in public land management that economic researchers have found should hardly be surprising. Efficient use of resources is seldom a main criterion in decisions made by public land managers. Rather, as political realists, their principal concern is to balance interest group pressures and to achieve an acceptable resolution among the many users of the public lands.

The Anomaly of Public Land Ownership

It is curious that public opinion in this country overwhelmingly opposes government ownership of most kinds of enterprises—steel mills, auto plants, banks, retail stores—but cares little that the federal government owns about half of the West. Indeed, it is only recently that

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economists and others have begun to ask the obvious question: why should land be an exception to the American consensus against government ownership?

Defenders of the current system have generally tried to throw the burden of proof onto their adversaries, by demanding a definitive demonstration that private ownership of western lands would be superior. Yet one would think that the burden of proof would more logically lie on them. Today, even many advocates of strong government involvement in the economy agree that the government generally does better to structure market incentives than to pre-empt or abolish the market. Thus, Charles Schultze of the Brookings Institution laments the previous tendency of activists "to see only one way of intervening—namely, [moving] a set of decisions from the decentralized and incentive-oriented market . . . to the command-and-control techniques of government bureaucracy," instead of "modifying the incentives of the private market."

There is no need to overstate the case by suggesting that in practice the private market achieves results that are close to some social optimum. It is enough to point out that its failings, substantial though they may be, have generally been fewer than the failings of public ownership.

The most common argument for federal ownership is that it protects fragile environmental and scenic values. But in our system of government, it has normally been regulation, not public ownership, that has been the procedure for guarding such values. *Private* land owners—many of whose holdings are intrinsically no different from the public lands—are forbidden to harm various sorts of wildlife, to strip-mine coal without taking environmental precautions, and so forth. If public land ownership is indispensable, it must be because there is some crucial regulatory objective that cannot be imposed on private landowners. If so, the question becomes: why ought not the government take over vast tracts of privately held land in the East—which hardly anyone wants it to do—in pursuit of the same objective?

If public land ownership is indispensable, it must be because there is some crucial regulatory objective that cannot be imposed on private landowners.

The best arguments for public land ownership apply only to that part of the public lands for which recreation or wilderness is the primary and most valuable use. In principle, it is possible for a private owner of such lands to charge high enough access fees to recreational users to keep the property both profitable and environmentally secure. In practice, however, the cost of collecting the fees might be too high, especially if the lands are widely dispersed. Moreover, wilderness might be a true "public good," valued by many persons who do not visit it. In either case, the public sector would have reason to step in to provide what the private sector will not. (The management of the land, however, might still be left in private hands. The private nonprofit sector has for many decades run a sizable preservation movement of its own.)

Even many of those who generally support federal retention of the public lands often acknowledge that a limited degree of privatization would produce more rational patterns of land ownership. Federal and nonfederal lands are closely intermingled in many areas of the West, reflecting historical accidents rather than considerations of efficient management. For example, large swaths of western land are held in "checkerboard" ownership, with the government and private owners each owning alternating sections of a square mile each—a legacy of the railroad land grants of the nineteenth century. Yet land uses such as livestock grazing and coal mining call for larger blocks of contiguous land.

Many federal holdings in the West are even smaller than one square mile. Some are in the midst of an urban area, others are surrounded by private rangeland and many are far from other federal holdings. There is little if any prospect that the federal government can manage these small parcels effectively. Indeed, the owners of the surrounding private land already typically graze their stock on these federal islands as though they were extensions of their own property.

The director of the Bureau of Land Management in the Carter administration, Frank Gregg, in 1982 advocated a major effort to re-

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solve this problem. He proposed to rationalize land ownership patterns by identifying parcels that should remain in federal multiple-use management, by evaluating and where desirable facilitating large-scale land swaps, and by identifying those public lands that might best be disposed of, either as trading stock for consolidating existing federal areas or by outright sale. While Gregg would doubtless not describe his "house-cleaning" proposal as a wholesale privatization scheme, it would result in sales of at least several million acres of federally owned lands, and possibly as much as 20 to 30 million acres.

From Idea to Action

In 1981 the idea of privatizing public lands had a well-developed theoretical rationale, but hardly any political constituency. Its base of support consisted of a few professors at places like Johns Hopkins University, Montana State University, and the University of Washington. These advocates undertook to transform the Sagebrush Rebellion into a movement to transfer federal lands not to the states, for free, but into private ownership. By the fall of 1981 they had achieved a respectful hearing among some key Sagebrush rebels. Indeed, in early 1982, rebel leader Dean Rhoads, a Nevada rancher and state assemblyman, stated that "[w]e've shifted positions drastically," in part because "we've had to face the hard fact that the Federal Government was not going to give one-third of America to the States for nothing." Rhoads called for privatization subject to the caveat that "if lands are sold, traditional rights and uses should be retained, such as recreation and hunting and fishing, to be managed by states."

The new movement soon found adherents within the Reagan administration. In October 1981 William Niskanen, a member of the President's Council of Economic Advisors, criticized the financial losses and inefficiencies of public land management and suggested selling "much of" the public land estate. A few months later, as a result of a meeting between presidential counselor Edwin Meese and President Reagan, it was decided that an effort to sell substantial areas of public lands would be included in a broader plan to sell off unneeded federal property in general.

In February 1982, the Cabinet Council on Economic Affairs presented to President Reagan a proposal for "promptly developing a program to dispose of unneeded public lands"—a program that would have to be tentative because it would most likely require "sweeping revisions in existing Federal laws and regulations." On February 25, 1982, Reagan signed an executive order establishing a Property Review Board reporting directly to the White House, with the function of identifying unneeded lands, buildings, and other facilities throughout the government and establishing procedures for their sale. On the same day, Director David Stockman of the Office of Management and Budget (OMB) testified to Congress that the public land part of the overall sale program would focus on "residual BLM land and limited Forest Service lands," and made it clear that national parks and other special areas were to be excluded. Explaining the reason for the program he noted:

> Some Federal holdings that were initially acquired at low cost have substantially appreciated in value because of changing land use patterns. The Government has not responded to changing market demands for alternative uses of land and structures as have private sector owners of real property. Government agencies continue to maintain operations on high value sites even though these operations could be relocated to lower cost areas without any negative effects on the program.

As an example, he noted that the BLM owns an 8,900-acre parcel five miles from the center of gold-plated Palm Springs, California. Stockman estimated that the Forest Service had at least 150,000 acres in "isolated ownerships, road right-of-way, and unintentional trespass situations" that could be sold.

Stockman made it quite clear that a basic purpose of the program would be to obtain revenue for the government. He tentatively proposed a revenue target from sales of surplus federal buildings and lands (other than those of the public land agencies) of $1 billion in 1983 and $2 billion a year in later years. He also indicated an intent, beginning in fiscal 1984, to raise an added $2 billion a year from sales of BLM and Forest Service lands. Thus, the program was supposed to raise about $17 billion in revenues over the next five years, around half

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of which were to come from public lands. The five-year target of $17 billion was later used by the administration and was picked up widely in press reports.

Stockman's testimony already showed the conflicting objectives that were to beset the privatization effort. On the one hand, the effort was defended as a way to clean house and improve efficiency. On the other hand, it was supposed to raise large amounts of revenue, with the purpose, as other administration statements made clear, of reducing the federal deficit. Yet the land plots that were most suitable for sale on efficiency grounds were not always those that would fetch the highest price tags. Moreover, the steps needed to gain political acceptance for the sales, such as excluding numerous categories of land and minimizing the likely disruptions resulting from land sales, all tended to lower the revenues the federal government could expect to receive.

Stockman's testimony already showed the conflicting objectives that were to beset the privatization effort. . . . the land plots that were most suitable for sale on efficiency grounds were not always those that would fetch the highest price tags.

The Interior Department's Response

The Property Review Board in early 1982 asked Interior, along with other federal agencies, to draw up plans for future land and property sales. Interior's plans, formally approved by the Property Review Board in May 1982, were based partly on field office canvasses classifying public lands into three categories. The first category included national park and wilderness areas, areas with known or suspected valuable mineral reserves, and others that would be permanently retained by the federal government. The second category consisted of land suitable for immediate sale or transfer. These lands were limited in total acreage and unlikely to provoke much controversy. They included urban sites potentially usable for residential or commercial development, small parcels of rangeland amidst nonfederal holdings, and lands with significant commercial, industrial, or farm potential. The third category consisted of land the department had marked for further study, which included —in the case of grazing lands—examining such alternatives as long-term leasing instead of outright sale.

Tables 1 and 2 show the land classified by acreage, estimated sale values, and state. Previous BLM land-use plans, mostly dating back before the Reagan administration, had already identified some 2.7 million acres suitable for sale with an estimated value of $2.0 billion. A further 1.7 million acres with an estimated value of $439 million were also deemed to be suitable for sale, but could not be sold until existing land use plans were amended. The 4.4 million acres in these two categories added up to less than 3 percent of the 175 million acres of BLM land in the contiguous forty-eight states. Twenty percent of the land identified for sale was in Nevada, 15 percent in Wyoming, and 14 percent in Arizona. The Nevada land amounted to only 1.5 percent of the 86.1 percent of that state held by the federal government.

Table 1
LANDS IDENTIFIED BY THE INTERIOR DEPARTMENT FOR SALE

Type	No Change in Land Use Plan Required		Changes in Plan Required	
	Acres	Value ($ millions)	Acres	Value ($ millions)
(1) Lands in urbanizing areas or with residential, commercial, or industrial value	485,989	$1,626	103,834	$100
(2) Farmable lands	451,202	130	294,342	84
(3) Lands uneconomic for federal management	1,525,642	253	1,255,598	242
(4) Lands no longer needed for federal purposes; disposal would serve other public purposes	244,180	67	92,769	10
TOTAL	2,707,013	$2,077	1,746,543	$438

Note: Surface value only (does not include mineral value).
Source: Interior Department estimates, 4/30/82.

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The field offices also identified another 27 million acres of BLM land in potentially fragmented ownership and put it in the "further study" category. Of these, 7.5 million acres were held in railroad checkerboard patterns, 9.6 million acres were located in townships (six-by-six-mile squares) in which the BLM owned less than 20 percent of all township land, and another 9.6 million acres were located in townships in which the BLM owned 20 to 40 percent of the land.

Interior Secretary James Watt was not one of the proponents of the privatization program. For one thing, it was originated outside Interior and thus raised a turf challenge. Moreover, because of its emphasis on revenue raising, it largely displaced his "good neighbor" policy of free or highly preferential land transfers to state and local governments, although the program would have given grandfather status to existing state applications for transfers. Watt also probably sensed the political liabilities that were soon to become apparent as the program developed.

Thus, at a White House press briefing, after again reassuring the press that "the National Parks, the wilderness areas, the refuge areas, the conservation areas will not be for sale," Watt emphasized that "at this time, we have no parcels of any real size that we are singling out. There will not be massive land transfers under this program." In later statements Watt added that no more than 5 percent of public lands would be sold. Since there are about 700 million acres of public lands, the cap on sales was widely reported in the press to be 35 million acres—even though, of course, the Interior Department had actually identified only 4.4 million acres of prime prospects for sale at that point. Even the higher figure, however, was not much higher than might well have resulted from Frank Gregg's proposal for a general house-cleaning of western land patterns.

Table 2

LANDS IDENTIFIED IN 1982 BY THE INTERIOR DEPARTMENT FOR SALE, BY STATE
(thousands of acres)

State	Urban	Farmable	Uneconomic for Federal Management	No Longer Needed, etc.	Total
Arizona	57.8	75.6	475.9	2.9	612.2
California	111.4	47.8	133.7	27.2	320.1
Colorado	20.8	19.2	347.5	2.2	41.1
Eastern states	12.5	0.9	42.4	0	404.4
Idaho	8.9	170.7	114.9	0.5	295.0
Montana	1.6	27.3	375.5	0	404.4
Nevada	275.5	241.4	154.0	214.1	885.0
New Mexico	30.8	5.2	409.0	3.5	448.5
Oregon	9.7	58.2	185.9	0.5	254.3
Utah	18.1	20.1	91.0	4.1	133.3
Wyoming	42.7	79.1	450.5	82.0	654.3
TOTAL	589.8	745.5	2,780.3	337.0	4,452.6

Source: Interior Department estimates, 4/30/82.

Whether the [projected sales] figure was 35 million acres, representing only 5 percent of the public lands, or 4.4 million acres, representing a minuscule figure smaller than one percent, it seemed like a very large absolute amount of land.

Belated efforts by the Reagan administration to minimize the scope of the proposed land sales were of little avail. Whether the figure was 35 million acres, representing only 5 percent of the public lands, or 4.4 million acres, representing a minuscule figure smaller than one percent, it seemed like a very large absolute amount of land. Furthermore, it would obviously take a lot of land sales to achieve the stated revenue target of $17 billion over five years (which, by the way, included sales of other properties along with public lands). To the press, moreover, a massive sale program made a better story than a modest one.

In July 1982, a front-page story in the *New York Times* opened with the statement, "the Reagan administration has begun what could be the most extensive transfer of public property and resources to private control in recent American history." The next month a *Time* mag-

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azine cover story on the "land sale of the century" reported that

> the scope of the proposed sales is enormous. . . . Both President Reagan and his Interior Secretary James Watt are convinced that the U.S. owns far more land than it needs or can manage. And both believe that unneeded land should be turned over to private owners.

As a result of such press coverage, the idea became firmly implanted in public attitudes that privatization was about to cut deeply into public land holdings—a seemingly drastic policy change that was to occur with little advance planning or debate.

The Rise of Opposition: Stockmen vs. Stockman

The cabinet council had warned that "altering present policies, either selling the lands or raising user fees, would likely generate considerable controversy." Among the potentially hostile groups were ranchers (unless they were allowed to buy the land for well below market value), environmental groups fearing large-scale development and a shift in environmental protection values, local communities that had been receiving federal lands for "public purposes" at less than fair market value, private landowners fearing that large federal lands sales would drive down the price of their own land, and hunters, fishers, and other recreational enthusiasts who had enjoyed free access to the land. The most powerful opposition came from what might be called the Subsidized Sagebrush. Not only were ranchers benefiting from below-market grazing fees, but in many cases they had literally invested in those rights by buying them from other ranchers. Grazing rights on public land are often attached to particular parcels of private land (and water) property, which consequently sell at a substantial premium, in some cases amounting to half or more of the private land value.

The most powerful opposition came from what might be called the Subsidized Sagebrush. Not only were ranchers benefiting from below-market grazing fees, but in many cases they had literally invested in those rights by buying them from other ranchers.

If public land was to be sold at full market prices, one of two things would happen. Existing public land users might buy the properties, in which case there would be a massive financial outflow from western states to the federal government. Or outside buyers might come in to buy the land, in which case existing users would either be displaced or would pay high rents. Either way, existing users would lose. Even the sales of urban lands and other odd parcels, while entailing few risks to the West per se, might have set a precedent for much larger land sales at full market value prices at some point in the future.

Privatization, like the Sagebrush Rebellion, also threatened to disrupt the political structure of the West. Most of the special political character of the West derives from the fact that nowhere else is the federal government so closely involved in matters of solely state and local concern. For example, in the 50 percent of the West that is federally owned, federal land managers play the role that local zoning authorities play elsewhere. If the federal managers left the scene, state governors, state legislators, and local officials would suddenly become more powerful figures. All of the relevant interest groups, which have built up a great deal of capital in learning how to deal with the existing system, would lose this investment and have to learn a new political system.

As these factors became more apparent, whatever early western support for the privatization effort had existed turned quickly to opposition. Ranchers and other traditional western land users joined with environmentalists and other national interest groups to derail the entire privatization effort. The *Nevada State Journal* reported on May 5, 1982, that "leading sagebrush rebels" in that state were seeking "to put as much distance as possible between their cause and privatization." Mining and livestock industry spokesmen sought to dispel what they said was the myth that ranchers and miners wanted to buy up federal lands. Actually, said Ned Eyre of the Nevada Cattlemen's Association and Bob Warren of the Nevada Mining As-

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Back-Door Rulemaking: A View from the CPSC

Terrence M. Scanlon and Robert A. Rogowsky

THREE YEARS AGO in these pages Antonin Scalia, now a U.S. appeals court judge, warned that the successes of the regulatory reform movement would have an unexpected and unwelcome consequence. As Congress and the White House redouble their efforts to control rulemaking by regulatory agencies, he said, they may simply be "squeezing the balloon of bureaucratic arbitrariness at one point, only to have it pop out somewhere else." The "recent encumberment of rulemaking" with extra procedural safeguards, he predicted, "will produce a renaissance of the previously favored mode of making law and policy—a movement back to basics, to adjudication."

In the years since then, there have emerged visible signs that the balloon is indeed popping out elsewhere—that there is a trend toward regulation by adjudication. Agencies are accomplishing more of their policy goals through the case-by-case proceedings in which they grant licenses, order product recalls, set back-pay awards, or otherwise apply the law to individual parties. The Consumer Product Safety Commission (CPSC) is a good example. While easing itself out of rulemaking, it is learning to use its adjudicatory powers to achieve the same results.

If this trend continues, the consequences for regulatory reform could be immense. Congress and the White House may find that they have been setting up checkpoints on an increasingly lonely road. They may, indeed, end up in full control of a procedural mechanism that has been abandoned by creative regulatory bureaucracies.

Terrence M. Scanlon is a member of the Consumer Product Safety Commission. Robert A. Rogowsky is his assistant.

CPSC Rulemaking Bogs Down

The Consumer Product Safety Act of 1973 originally envisioned that rulemaking, which applies to products generically, would be the commission's primary tool for regulating consumer safety. It soon became clear, however, that the commission was not going to produce as many rules as had been expected. The first chairman of the CPSC forecast that the commission would enact twenty mandatory safety standards a year. The commission itself promised to initiate forty standard-setting proceedings in 1975 alone. The plan was to promulgate 100 mandatory product safety standards between

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1977 and 1982. By 1978 the agency actually had promulgated only three.*

Disenchanted with this performance, Congress at first took steps to make rulemaking easier. The 1978 amendments to the Consumer Product Safety Act relaxed unrealistically tight procedural deadlines as well as a cumbersome requirement that had forced the commission to rely on outside groups' offers to develop proposed standards.

Three years later, however, Congress reversed itself in the Product Safety Act Amendments of 1981. These amendments hem in CPSC rulemaking in several ways. First, they add an extra initial step to the agency's rulemaking process in the form of an "advance notice of proposed rulemaking." Second, paralleling a key provision of Executive Order 12991, they require the commission to analyze the costs and benefits of its proposals, both at the beginning of the rulemaking procedure and later after all the evidence has been gathered. These analyses must also identify the parties "likely to receive the benefits and bear the costs" of the rule and explain why alternatives were not adopted.

Third, the 1981 amendments restrict rulemaking in a number of more specific ways. The commission must now defer to a voluntary standard being adopted by an industry, for instance, if that standard is likely to reduce the risk adequately. Moreover, the commission may not issue a rule on a chronic health hazard until an expert advisory panel nominated by the National Academy of Sciences has made a report on the available evidence.

In addition, rulemaking at the CPSC is subject to a variety of constraints that apply to other agencies as well. For example, the commission must analyze the effects of its rulemakings (but not adjudications) on small business (under the Regulatory Flexibility Act of 1980) and the environment (under the National Environmental Policy Act of 1969).

All these extra requirements make rulemaking an even less attractive pursuit than it was in the 1970s. Indeed, the informal consensus in the agency is that rulemaking is dead; it simply takes too much effort. The CPSC has started only one substantive rulemaking since 1981, and it later withdrew that one in favor of a voluntary standard. No others appear to be coming along. This is not to suggest that the agency is inactive, only that its activity is taking a different form. The balloon has popped out elsewhere—in adjudication.

Regulating Children's Products

The trend toward adjudication is reflected in the commission's growing tendency to transfer products from its jurisdiction under the Hazardous Substances Act, which generally requires it to conduct a rulemaking before banning a product or ordering a recall remedy, to the Product Safety Act, which allows it (in addition) to proceed by adjudication in many of the same circumstances. The adjudicatory powers conferred by the Product Safety Act are strong. The commission can demand the recall of a product, including its replacement or refund, on the ground that it suffers from some sort of "defect"—a term the act does not define.

Initially the commission could transfer a product to the Product Safety Act only if the regulatory powers available under the Hazardous Substances Act were "inadequate to eliminate or reduce the hazard to a sufficient extent." However, finding the rulemaking procedures of the Hazardous Substances Act to be onerous—a rulemaking to set standards for fireworks dragged on for three years—the commission requested an easing of the transfer provision. Congress complied in 1976, requiring henceforth only that the transfer be in the "public interest"—a term it did not define and whose interpretation has rested with the commission itself. This virtually unlimited transfer power allows the commission in practice to use the strong adjudicatory powers of the Product Safety Act against the whole range of consumer products in its jurisdiction.

An example of the new trend is the regulation of toys and children's products. Since 1981 the commission has transferred five separate children's products from the Hazardous Substances Act to the Product Safety Act for litigatory action: (1) stuffed toys with looped string

*The total has now risen to six, but major portions of two have been struck down by the courts. The commission also has imposed two labeling requirements and six product bans under the Product Safety Act, one of which was overturned by the courts. The commission can claim credit for five more rules under the Federal Hazardous Substances Act and requirements for child resistant caps for several products under the Poison Prevention Packaging Act.

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that posed a strangulation hazard; (2) squeeze toys that could become impacted in the throat; (3) mesh-sided cribs that presented a suffocation hazard; (4) expandable enclosures ("corrals") in which children could be strangled; and (5) crib hardware that, if missing or not functioning properly, could allow cribs to collapse. In the case of mesh-sided cribs and expandable enclosures, the commission filed complaints naming as defendants every manufacturer of the type of product in question, thus using adjudication in the way that most closely mimics rulemaking.

Each of the other children's product cases similarly addresses not a hazard peculiar to one manufacturer, but an industry-wide generic product condition—the sort of situation that the commission has traditionally and appropriately addressed by rulemaking. For example, when the commission learned in 1981 that children could choke on some squeeze toys, it moved to recall not just toys of the specific manufacturers or designs that had been implicated, but all toys of a general description. Likewise, when the commission recently moved to regulate crib hardware, using the threat of its adjudicatory powers, its concerns had to do with general design and material standards, not defects specific to one manufacturer.

The reason all five of the children's products were transferred to the Product Safety Act was to allow adjudication. As the CPSC noted in its *Federal Register* notice covering the squeeze toy transfer, corrective action would be available under the Hazardous Substances Act "only if the commission had first issued a rule under provisions of [that act]." By contrast, under the Product Safety Act "no requirement for rulemaking would exist in order to invoke the [recall] provisions . . . of that Act." The proposed Child Safety Act of 1984, currently pending before Congress, would add adjudicatory authority to the Hazardous Substances Act, thereby eliminating the need to transfer.

Problems with Adjudication

In principle, both rulemaking and adjudication provide procedural safeguards for affected parties—rulemaking through its notice and comment procedures, adjudication through a hearing before an administrative law judge. Both also provide for full consideration of all relevant information. But the practical differences are important.

In a rulemaking, the agency notifies the public of its interest in a particular safety hazard and then gathers evidence to enable it to assess the severity of the hazard and determine the appropriate remedy. All interested parties —regulators, consumers, and producers—help create the body of evidence on which the regulatory decision will be based. The procedure is designed, as the Supreme Court noted fifteen years ago, "to assure fairness and mature consideration of rules of general application" (*National Labor Relations Board* v. *Wyman-Gordon Co.*, 1969). Rulemaking is also prospective in its scope and its remedies: targets are given fair warning that the law is changing.

In an adjudication, the agency files an administrative complaint against a firm or firms. Other affected parties, if they learn of the litigation at all, can intervene (an option that is limited to parties materially and adversely affected) or file an amicus curiae brief. This does not provide as much scope for complicated technical comments or input from the general public as does a rulemaking procedure. Adjudication is also, by nature, retrospective—that is, it penalizes a firm for its conduct during a period before the agency acted, conduct that in many cases was legal at the time.

Although the target of an adjudicatory complaint enjoys due process protection (since it does get its day in court), in other ways it comes off worse than it would in a rulemaking. If it can afford to contest the charge at all, it may still find its reputation badly damaged. The closer the agency gets to issuing a complaint or taking the case to trial, the more likely that the toy manufacturer, for example, will read accusations in the press that its products are "child-killers." It is no wonder that more than 98 percent of the CPSC staff's preliminary allegations of substantial product hazards are settled "voluntarily" before a complaint is issued.

Consider that last fact. One of the features of adjudicatory actions at the CPSC is that they are almost always settled through negotiation —which, of course, has many advantages over no-holds-barred litigation in court. Note, however, that although the full commission must approve a decision to proceed with litigation, it does not pass on the prior staff decision to

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threaten litigation. Yet such a threat is usually all that is needed to produce an industry-wide standard. If the staff presents as a *fait accompli* a settlement to which manufacturers have already consented, an overworked commission is likely to go along.

Thus, negotiation may allow the commission's legal staff to bypass effective review by the commission and all the restrictions on rulemaking as well. This can have important consequences. For example, the 1981 amendments to the Product Safety Act call on the CPSC to pursue "performance" rather than "engineering" standards. But a negotiated settlement can easily and legally take the form of an engineering standard. This happened recently when the commission negotiated an engineering fix with a group of cabinet heater manufacturers to settle a product defect allegation.

Another problem is that manufacturers may be uncertain as to the scope of the implicit product standard embodied in the negotiated settlement or litigated outcome. The Supreme Court recognized in *Wyman-Gordon* that adjudicated cases generally provide a

> guide to action that the agency may be expected to take in future cases. . . . But this is far from saying . . . that commands, decisions, or policies announced in adjudication are 'rules' in the sense that they must, without more, be obeyed by the affected public.

What if a manufacturer not included in the litigation refuses to accept the implicit product standard, perhaps on the view that it has invented a safe version of the generically banned product? The only way for the agency to resolve the issue is to file a separate complaint. Note, however, that the firm that agreed to the original negotiated settlement is the only one that may not try to market such an invention, a fact that might subject it to a distinct competitive disadvantage.

The greater flexibility of "adjudicative rulemaking" from the agency's standpoint can create even more uncertainty about the state of the law. Agencies have considerable latitude to disregard their prior adjudicative decisions, whereas they are legally forbidden to depart from their regulations. If a safety standard is set by rulemaking, the agency may subsequently change it only by a new rulemaking, with much advance warning. But if the standard is set by adjudication, the agency has more alternatives. It can attempt to expand the standard by filing charges against some manufacturer which thought it had been complying with the law. Or it can relax or abandon the standard simply by letting it be known that it does not intend to file any more cases in those circumstances. The new "standard" that results may meet nobody's needs or interests but those of the agency's.

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Finally, the safeguards of rulemaking also tend to rein in an agency that is ignoring public opinion or the public interest. As Justice William Douglas wrote in his dissent in the *Wyman-Gordon* case:

> The multiplication of agencies and their growing power make them more and more remote from the people affected by what they do and make more likely the arbitrary exercise of their powers. Public airing of problems through rule making makes the bureaucracy more responsive to public needs and is an important brake on the growth of absolutism in the regime that now governs all of us.

NOT TOO LONG AGO, rulemaking was held out as the great hope for public-spirited regulation, a technique that would avoid the inherently confrontational nature of litigation and instead draw industry, consumers, and the agency into a collaborative effort to everyone's benefit. As it turned out, rulemaking led to a variety of problems. The very sweep of the power it gave the agencies frequently encouraged their tendencies toward social engineering. But it would be a shame to abandon the virtues of broader public input by moving from a rulemaking process now reformed to an adjudicatory process that remains unreformed. Whatever shape it takes or whatever name it carries, much of regulation is in effect legislation. It should not be isolated from the political process. ■

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From Bad to Comparable Worth

Charles Krauthammer

THE LATEST ENTRY on the list of sacred liberal causes is comparable worth. According to that doctrine, it is demonstrable that low-paying female-dominated jobs, like nursing, are worth as much (to employers or society) as "comparable" male-dominated jobs, like plumbing, and that therefore by right and by law they should be paid the same. Comparable worth has become not only *the* women's issue of the 1980s but also the most prominent civil rights issue not specifically directed at blacks. The Democratic party has warmly embraced it. Every one of its presidential candidates has endorsed it. In the 1984 platform, that sea of well-intended ambiguity and evasion, there are few islands of certainty. Comparable worth is one of them.

Comparable worth is advancing in the courts, too. Three years ago the Supreme Court opened the door a crack by ruling, in *County of Washington* v. *Gunther*, that female prison guards could sue for violation of the equal-pay provisions of the 1964 Civil Rights Act, even though they did not do precisely the same work as the better-paid male prison guards. That narrow ruling was broken open last December in a sweeping victory for comparable worth in Washington State. In *AFSCME* v. *State of Washington*, a federal district judge found the state guilty of massive discrimination because its female-dominated jobs, though paying a market wage, were paying less than "comparable" male-dominated jobs. He ordered an immediate increase in the women's wages and restitution for past injury. The back pay alone will run into the hundreds of millions of dollars.

COMPARABLE WORTH MAY INDEED be an idea whose time has come. Where does it come from? When the plumber makes a house call and charges $40 an hour to fix a leak, the instinct of most people is to suspect that the plumber is overpaid—the beneficiary of some combination of scarce skills, powerful unions and dumb luck. The instinct of comparable worth advocates, by contrast, is to see the plumber's wage as a standard of fairness, to conclude that the rest of us (meaning: women)

Charles Krauthammer is senior editor of The New Republic, *in which an earlier version of this piece appeared.*

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are underpaid, and to identify discrimination as the source of that underpayment. But since overt discrimination on the basis of sex has been legally forbidden for twenty years, to make that charge stick nowadays requires a bit of subtlety.

One claim is that women's wages are depressed today because of a legacy of past discrimination: namely, the "crowding" of women into certain fields (like nursing, teaching, secretarial work), thus artificially depressing their wages. Did sexual stereotyping really "crowd" women into their jobs? Sexual stereotyping worked both ways: it kept women in, but it also kept men out, thus artificially excluding potential wage competition from half the population, and, more important, from about two-thirds to three-quarters of the labor force (because of the higher participation rate of men). Sex-segregation is obviously unfair, but it is hard to see how it caused downward pressure on women's wages when, at the same time, through the socially enforced exclusion of men, it sheltered "women's work" from a vast pool of competitors. Moreover, as the social barriers that kept men and women from entering each other's traditional fields have fallen during the last twenty years, there has been much more movement of women into men's fields than vice versa. "Women's work" is less crowded than ever.

If the crowding argument is weak, then one is forced to resort to the "grand conspiracy" theory. "The system of wages was set up by a grand conspiracy, so to speak, that has held down the wages of women to minimize labor costs," explained the business agent of the AFSCME local that in 1981 struck for and won a famous comparable-worth settlement in San Jose. But since to minimize labor costs employers try to hold down the wages of everyone, the thrust of the argument must be that there is a particular desire to do so additionally in the case of women. In other words, the market is inherently discriminatory. Women nurses are paid less than they deserve, simply because they are women. How to prove it? Comparing their wages to that of male nurses won't do, since their pay is, by law, equal. So one must compare nurses' wages to that of, say, plumbers, show that nurses make less, and claim that nurses are discriminated against because they deserve—they are worth—the same.

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What is the basis of that claim? In San Jose, Washington State, and other comparable worth instances, the basis is a "study." A consultant is called in to set up a committee to rank every job according to certain criteria. In Washington State, the "Willis" scale gives marks for "knowledge and skills," "mental demands," "accountability," and "working conditions." The committee then awards points in each category to every job, tallies them up, and declares those with equal totals to have—*voilà!*—comparable worth.

There is no need to belabor the absurdity of this system, so I'll stick to the high points. It is, above all, a mandate for arbitrariness: every subjective determination, no matter how whimsically arrived at, is first enshrined in a number to give it an entirely specious solidity, then added to another number no less insubstantial, to yield a total entirely meaningless. (An exercise: compare, with numbers, the "mental demands" on a truck driver and a secretary.) Everything is arbitrary: the categories, the rankings, even the choice of judges. And even if none of this were true, even if every category were ontologically self-evident, every ranking mathematically precise, every judge Solomonic, there remains one factor wholly unaccounted for which permits the system to be skewed in any direction one wishes: the *weight* assigned to each category. In the Willis scale, points for "knowledge and skills" are worth as much as points for "working condi-

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tions." But does ten points in knowledge and skills make up for ten points in hazardous working conditions? Who is to say that a secretary's two years of college are equal in worth to—and not half or double the worth of—the trucker's risk of getting killed on the highways? Mr. Willis, that's who.

Conclusions based on such "studies" are not a whit less capricious than the simple assertion, "secretaries are worth as much as truck drivers." Trotting out Willis, of course, allows you to dress up a feeling in scientific trappings. It allows H.R. 4599, Representative Mary Rose Oakar's bill legislating comparable worth in federal employment, to dispose of the arbitrariness problem in the *definitions*. "Job evaluation technique" is defined as "an objective method of determining the comparable value of different jobs." Next problem.

Equal Pay for Potential Work?

A number of advocates of comparable worth, aware of this objectivity conundrum and perhaps less confident that it can be defined out of existence, propose an alternate solution. Instead of ranking the intrinsic worth of the *job* (by admittedly arbitrary criteria), they propose ranking the worth of the *worker*. Barbara Bergmann, an economist at the University of Maryland, believes that people with similar qualifications, training, and experience should be receiving the same return on their "human capital." Breaking new ground in discrimination theory, she claims that "in a nondiscriminary setup, identical people should be paid identically." And what makes people identical? Their credentials: qualifications, training, experience. This is not just credentialism gone wild, and highly disadvantageous to non-yuppy workers with poor resumes, who need the help of the women's movement the most; it leads to the logical absurdity that people should be paid not for the actual work they do, but for the work they *could* do. We've gone from equal pay for equal work, to equal pay for comparable work, to equal pay for potential work. Summarizing the Bergmann position, the newsletter of the Center for Philosophy in Public Policy at the University of Maryland explains helpfully that "if a nursing supervisor could do the work of a higher-paid hospital purchasing agent, then her wages should be the same as his." But why stop there? What if her credentials are the same as those of the hospital administrator, or her city councilor, or her U.S. senator? And what about the starving actress, waiting on tables for a living? If she can act as well as Bo Derek (to set a standard anyone can meet), shouldn't she be getting a million dollars a year—that is, if the "setup" is to deserve the adjective "nondiscriminatory"?

Now, even if there were a shred of merit in any of these systems for determining comparable worth, we should be wary of implementing them if only because of the sheer social chaos they would create. The only sure consequence of comparable worth one can foresee was described by the winning attorney in the Washington State case: "This decision . . . should stimulate an avalanche of private litigation on behalf of the victims of discrimination." The judicial and bureaucratic monster comparable worth will call into being—a whole new layer of judges, court-appointed "masters" (there already is one in the Washington State suit), lawyers, and consultants—will not just sit once to fix wages and then retire. The process will be endless. Fairness will require constant readjustment. There will still exist such a thing as supply and demand. Even if comparable worth advocates succeed in abolishing it for women's work (remember, Washington State was found to have broken the law for paying women market wages rather than comparable worth wages), it will still operate for men's wages, the standard by which women's (comparable worth) wages will be set. Now, what if nurses are awarded plumbers' pay, and there develops a housing slowdown and a plumber surplus, and plumbers' wages fall? Will nurses' salaries have to be ratcheted down? And if not, what is to prevent the plumbers from suing,

The process will be endless. Fairness will require constant readjustment. There will still exist such a thing as supply and demand . . . for men's wages, the standard by which women's (comparable worth) wages will be set.

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alleging they are underpaid relative to comparably equal nurses?

Which brings us to the equity problem. Almost everyone feels he or she is underpaid. Moreover, even a plumber can point to at least one person or group of persons who are getting more than they are "worth." Why can't he claim that class of people as the equitable standard, and march to court demanding restitution? If comparable worth is simple justice, as its advocates claim, why should only women be entitled to it? Why not comparable worth for everyone?

The whole search for the "just wage," which is what comparable worth is all about, is, like the search for the "just price," inherently elusive in a capitalist system. It is not that justice has nothing to say about wages and prices in a market economy, but that what it does say it says negatively. For example, it declares that whatever the wage, it must be the same for people regardless of sex, race, or other characteristics; but it doesn't say what the wage should be. Even the minimum-wage law says merely that a wage may not be below a certain floor. (Even capitalism has a notion of exploitative labor.) Beyond that, the law is silent. The reason it is silent, the reason we decide to let the market decide, is no great mystery. It was first elaborated by Adam Smith, and amplified by the experience of the Soviet Union and other command economies. Market economies are agnostic on the question of a just wage or a just price not simply because of a philosophical belief that the question, if it is a question, is unanswerable, but also because of the belief, and the experience, that attempts to answer it have a habit of leaving everyone worse off than before.

Finally, even granting that women in traditionally female jobs are underpaid, it is not as if we live in a fixed economy which blocks off all avenues of redress. If secretaries are indeed paid less than they are "worth," they have several options. One is suggested by Coleman Young, the mayor of Detroit, a former labor leader and no conservative: "If a painter makes more than a secretary, then let more women be painters. Equal opportunity and affirmative action is how you do that." A woman entering the labor force today has no claim that she has been crowded into low-paying professions because of discrimination. She has choices.

Older women, of course, who have already invested much in their professions, are more constrained. But they have the same avenues open to them—such as organizing—as other similarly constrained (predominantly male) workers who struggle for higher wages in other settings. In Denver, for example, nurses sought comparable worth wage gains in court and lost; they then went on strike and won. True, in some occupations, even strong unions can't raise wages very much. But as the president of the International Ladies Garment Workers Union (85 percent female) explained in objecting to a highfalutin AFL-CIO endorsement of comparable worth, the problem is not discrimination but the market. His workers have low wages because they compete with workers overseas who are paid thirty cents an hour. Comparable worth doctrine may declare that garment workers ought to be making as much as truck drivers. But if the theory ever became practice, garment workers would be free of more than discrimination. They would be free of their jobs.

WHY IS THE OBVIOUS about comparable worth so rarely heard? Why is it for liberals the ultimate motherhood issue? Because here is a class of people who feel they aren't getting their just due, blame that condition on a single cause (discrimination), then offer a "rational" solution, on whose messy details they prefer not to dwell. But those details add up to a swamp of mindless arbitrariness and bureaucratic inefficiency, shrouded in a fine mist of pseudo-scientific objectivity. And the surest results will be unending litigation and an entirely new generation of inequities. These inequities, moreover, will be frozen in place by force of law, and thus that much more difficult to dislodge.

Comparable worth asks the question: How many nurses would it take to screw in a lightbulb? The joke is that, having not the faintest idea, it demands that a committee invent an answer, that the answer become law, and that the law supplant the market. Even Karl Marx, who also had legitimate complaints about the equity of wages set by the market, had a more plausible alternative. ■

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for distributing SPR oil. The advantage of this system is that the draw-down of the SPR would begin slowly, in response to true market forces, rather than all at once after a political SPR draw-down decision was made. This approach might significantly dampen initial panic purchases of oil and hold down short-range oil price increases.

W. J. Montgomery,
Standard Oil Company (Indiana)

TO THE EDITOR:

Although it is desirable to add to the Strategic Petroleum Reserve, a tax on oil imports is not a good way to raise money for this purpose. Such a tax would make all oil products more expensive, and the higher cost of heating fuel would be particularly burdensome to the poor and to residents of the New England and other northern states. Furthermore, by depressing crude oil prices abroad, it would aggravate the foreign debt problems of many oil-producing countries, and probably stir up resentment abroad and strengthen the influence of the militant members of OPEC.

The excise tax on gasoline was recently raised from four to nine cents per gallon. If only two cents of this increase were designated to finance the SPR, it would support a fill rate of about 200,000 barrels per day. That is not only higher than the current rate, but higher than the 186,000 barrels-per-day rate that Congress would appear to be advocating.

As the authors note, it is important to establish in advance definite procedures that would make the SPR promptly available during any future disruption. They propose selling options to purchase SPR oil in advance. Before an emergency develops, however, it is most unlikely that enough options or futures contracts on SPR oil could be sold to make any difference in the market. The purchase of such contracts would entail significant costs that could hardly be justified in today's highly competitive crude oil markets. After an energy emergency has begun, of course, there is obviously no longer any need for sales of SPR options or futures. A better solution would be to sell SPR oil to U.S. refiners by public auction for current delivery only.

The authors also propose a system of emergency subsidies for those who suffer hardships during an oil disruption. This scheme attempts to solve an energy and a welfare problem simultaneously and winds up with second-best solutions for each. The revenues from the sale of SPR oil should be used to replenish it in the future. If persons on welfare need additional support to cover the increased costs of heating oil, food, or clothing, those funds should be provided from the traditional sources.

W. D. Hermann,
Chevron Corporation

GEORGE HORWICH and DAVID LEO WEIMER respond:

We welcome Rep. Synar's views, most of which are consonant with our own desire to rely on market forces. We have serious reservations, however, as to the IEA sharing agreement, which we believe would substitute mandatory allocation of oil for market distribution on the international level. We would also counsel against directed sales of SPR oil, other than to meet our IEA sharing obligations. In general, individuals or groups that are deemed worthy of assistance should receive cash grants, not oil. Directed sales do not promise greater efficiency and could initiate a general slide into allocations of oil at below-market prices throughout the economy.

We do not understand the basis for W. D. Hermann's claim that companies will find it prohibitively expensive to buy options on SPR oil. We would expect a well-designed options market to entail trivial transactions costs. The stringent product specifications of a futures contract, referred to by Rep. Synar, are not relevant to the sale of options. Given the flexibility of U.S. refineries, allowing a wide universe of primary and secondary buyers would assure that SPR oil of any grade, obtained through options, would eventually find its way to an optimum use.

There is merit in W. J. Montgomery's suggestion that SPR sales be conducted continuously at a price fifty cents to a dollar per barrel above the current market price. We do not believe the actual details of an automatic drawdown device are as important as the principle that it be in place.

The general case for an import fee to fund the SPR is that there is a national security premium not reflected in the market price of unstable imported oil. Others have explored this subject at length; our proposed $2 fee is at the bottom of the range of premium estimates. The fee will not, as Montgomery fears, lead to a differential between the prices of domestic and imported oil and thus to lobbying for entitlements to the lower-priced oil. There will be one common price for the entire oil market.

If, as is likely (especially in the present soft market), the fee reduces the world price, there will be losers as well as gainers, as Hermann points out. Previous analyses, however, have invariably found a net gain to consuming countries from any price decrease. Montgomery's suggestion that exporting countries will somehow retaliate against a U.S. tariff is not supported by conventional economic theory or the history of oil markets.

Our prediction of higher revenues from the windfall profits tax following imposition of a tariff was not meant to imply, as Ben Zycher infers, that the former tax is in any way desirable. In fact, we believe the misnamed windfall tax is highly inefficient and should be phased out as soon as possible.

The fact that the SPR benefits society at large, not just consumers of imported oil, does not, as Zycher argues, justify funding it through a general tax. Applying the tax to imported oil internalizes the costs of future disruptions, the mitigation of which constitutes the social benefit in question. Zycher's argument is analogous to calling for non-polluters to share in the costs of anti-pollution measures on the grounds that they benefit from the resulting cleanup.

Zycher confounds oil price drag with the resource reallocation dictated by higher relative prices of energy. The drag is a temporary but potentially damaging siphoning of funds into the coffers of the petroleum industry or financial institutions from other markets and industries. The empirical evidence indicates that oil price drag is at most a moderate deflationary force. But it *is* deflationary, and a moderate easing of monetary policy would serve to offset the fall in prices, not to raise them. At the same time, the massive permanent reallocation of resources that the higher relative price of energy induces would almost certainly be facilitated by a slight inflationary bulge. We believe there is a limited tradeoff between inflation and unemployment in transitional periods.

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Robert Weiner cites, as evidence of market failure, the tendency of spot market prices to rise above contract prices during disruptions. An alternative interpretation is that the usual excess of contract prices over spot prices during stable periods reflects in effect an insurance premium, assuring buyers of some future supply, and that this insurance is effectively cashed in during disruptions. That would be a symptom not of market failure, but of the market at work. One should not, however, take at face value the full difference between contract and spot prices during disruptions. Recent studies indicate that there are many non-price features of modern contracts that make the effective contract price higher than the nominal contract price during shock periods.

Weiner also sees market failure in the lack of "access" to crude oil supply experienced by small refiners and others during disruptions. His implicit assumption is that in a functioning market all buyers would undergo equal proportionate supply reductions. Again the market reality is more complex. Demand elasticities vary widely among petroleum products. The heavier output in which smaller refineries tend to specialize (boiler fuel, heating oil) has a higher demand elasticity and thus tends to undergo a greater reduction of demand when prices rise than does the lighter output (such as gasoline) that is more typical of larger refineries. The result is that disruptions reduce the relative economic power of small refineries to bid successfully for crude oil.

Ignoring these relationships, as Weiner does, leads to corrective policies (of which Weiner has a whole bagful) that destroy efficiency and exacerbate the costs of oil shocks—exactly as in the 1970s.

Video Copying

TO THE EDITOR:

Your "Perspectives" piece entitled "Betamax Goes Free" (*Regulation*, January/February 1984) was wide of the mark; the majority opinion in *Betamax* was correct on the merits. As patent law has evolved, *contributory* infringement can only be predicated on the sale of an article which has no other use than to infringe. In contrast, a "staple" item cannot be forced off the market in this way, for then purchasers would be deprived of a product that has some admittedly legitimate functions. Holding Sony liable on this basis is equivalent to finding Seagrams liable because some of its customers drive after drinking.

There is, however, a theory that could have suited the purposes of those who regard "time shifting" or "librarying" as a threat to the economic well-being of movie studios and the like. Section 271(b) of the

patent statute states that "whoever *actively induces* infringement . . . shall be liable as an infringer. . . ." Like the doctrine of contributory infringement, this doctrine could have been extended from the patent to the copyright context. As the district court opinion pointed out, Sony's ads urged users to "record favorite TV shows" and "build a library." Even so, the plaintiffs could not have prevailed unless they had established that such uses were unlawful.

More important is a point that was neglected by both minority and majority, the ninth circuit, and your article, namely that no *user* of video recorders was represented in the Betamax litigation. I fail to see how a court could, consistent with our notions of fair play, hold any user of a video recorder to be exceeding the bounds of "fair use" when no such user was more than nominally present in the litigation. The only individual user named as a defendant, William Griffiths, was (1) recruited by the plaintiff's law firm and (2) unrepresented in the litigation! I shudder to think of the long-term implications if this procedural device were to become common in resolving our rights and liabilities.

Thomas G. Field, Jr.
Franklin Pierce Law Center

THE EDITORS respond:

Field apparently believes that we have accepted the view of the *Betamax* minority that the manufacturers of recorders can be guilty of contributory infringement when their customers employ the equipment to infringe a copyright. Instead we simply reported the disagreement between the majority and minority opinions on this issue. Moreover, the theory that Field argues could have been used to find Sony guilty—that it induced infringement by others—was in fact advanced by the court's minority.

As we reported, Universal named a token individual as a defendant. But it is not entirely clear how Universal could have done otherwise. Would it have had to sue all individual users of videocassette recorders, or would some users have been assumed to represent their class? If the latter, how would the representatives be chosen? And who would have to pay the legal fees?

If the Supreme Court majority had held simply that Universal had brought the wrong defendant to the bar, the case could have stood for the proposition that Field is apparently advancing. If the court had held only that time-shifting was fair use, or that manufacturers of recording equipment would not be liable for their customers' infringements, the decision would similarly have had limited impact. But the majority's extended limning of the rights of "noncommercial" users, its requirement that copyright holders demonstrate that they have been harmed by such use, and its narrow view of what constitutes such harm, all suggest that the creators of intellectual property will have some tough times ahead no matter whom they pick as a defendant.

Coal Leasing Scandals

TO THE EDITOR:

Your discussion of the Commission on Fair Market Value Policy for Federal Coal Leasing ("The Coal Leasing Scandals," Perspectives, March/April 1984) is the best I have seen. It notes the key problem—that the commission was a short-term educational venture in which four of the five commissioners themselves needed tutoring. How-

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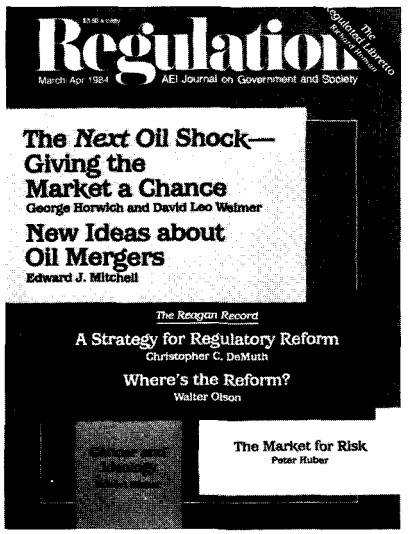
ever, you do not fully succeed in describing the convoluted process in which we on the commission were engaged.

One major issue was whether the Interior Department received fair market value on the Powder River Basin lease sales. The prior estimates of the fair market value of the tracts had been padded outrageously, and I felt any estimates of lost revenue ought to take into



account all sources of errors, not just those attributable to the Watt managers. Others wanted to include a stronger condemnation of the conduct of the program. Moreover, I felt then and feel more strongly now that the question of how much revenue the department lost on the Powder River sales was the wrong one to stress; the more important question was how to make leasing procedures sounder in the future. The resulting discussion of the Powder River sale in the commission report reflects a compromise among diverse positions, hammered out in exceedingly unfavorable circumstances.

At the last minute, previously confidential Inspector General reports suggesting wrongdoing were suddenly released. The commission staff had to draft and redraft its final report, without time to digest the new material thrown at it, under great pressure from an unreasonable deadline. (The chairman of the commission pushed with what I and others considered undue haste to complete the report.) The enemies of coal leasing made much of the report's failure to stress a few allegedly damaging data. Given the stresses, however, the surprise is that the report achieved the coherence and moderation it did.

It is hardly surprising that your article did not sort this all out. I was more startled to find you making some statements that seem unduly favorable to existing leasing policy.

First, you say that the process of estimating fair market value "involves two symmetric dangers: the price may be too low, giving the bidder an undeserved windfall, and the price may be too high, preventing the sale from taking place." In fact, these dangers are not symmetric. Overvaluing imposes real costs on the economy by preventing more efficient production. Undervaluing causes only a (probably modest) transfer of income to the bidder.

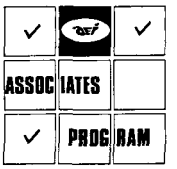
Second, you complain about the limited competition for coal leases. I am not sure that this problem would be a serious one if not for the current diligence requirements (which require companies to forfeit their leases unless they develop them within ten years). If companies in particularly advantageous positions really place unduly low bids, speculators can step in to bid up prices—except that the diligence requirement makes such speculation dangerous. The commission's reform program includes a loosening of this anticompetitive restraint; the next logical steps should be to remove the mass of limits on the permissible coal holdings of individual companies and replace the current royalty-per-ton system with an exclusive reliance on the initial bidding for leases themselves.

Richard L. Gordon,
Pennsylvania State University

THE EDITORS respond:

Gordon is reading us too literally if he interprets our use of "symmetric" to mean that the dangers of undervaluing and overvaluing are precisely the same. Our point was simply that there are dangers on both sides; it was meant as a corrective to the too-common view that undervaluation is the only real hazard.

The hazards of undervaluation, however, may go beyond the distributional concerns Gordon describes. Under a variety of plausible assumptions, undervaluation could lead to economic inefficiencies in the bidding process, the production process, or both. ■



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Race, Ratchets, Redistricting, and the Voting Rights Act
(*Continued from page 13*)

ture had divided part of Dallas into two congressional districts, each with a black population of 40 percent, thus securing the seats of two incumbent white liberal Democrats. Blacks, supported by Republicans, took the plan to court, seeking the creation of one overwhelmingly black district and one overwhelmingly white district. The district court refused to alter the lines, however, because the incumbent members of Congress, in the court's words, had "strong records of support for the concerns of black voters." Adopting the plaintiff's scheme would presumably result in retrogression to a state where only one of the two members possessed such a record.

This solicitude for nonminority candidates believed sympathetic to minorities cropped up in another recent case. In mid-1983 the Justice Department had vetoed the creation of a new school district in Madison and Ridgeland, Mississippi, two fast-growing suburban towns outside Jackson. After their initial plan was rejected, the local authorities in Ridgeland passed a law providing that one of three appointive slots on the new board would automatically go to a black. The Justice Department apparently balked, because after lengthy negotiations the authorities modified their submission, saying they would guarantee the slot not to a black, but to a person who is "representative of minority interests." This formulation won approval in the summer of 1984.

The principle behind this line of rulings is that the act requires the election or appointment of, not minority candidates, but candidates who hold views that are presumed to be congenial to minorities. Rather than a racial test for office, this establishes what amounts to an ideological test.

That raises an interesting problem. The black plaintiffs in the Mississippi case want a firm rule of law entitling them to a 65 percent majority wherever it is possible to draw such districts. Yet this standard would undoubtedly endanger the seats of liberal white candidates around the country. The drive for proportional representation, in other words, conflicts with the drive toward judicial and executive promotion of candidates deemed racially progressive.

It is worth noting, by the way, that the same sorts of boundary lines that are disfavored by the courts in legislative districting cases are strongly encouraged in school districting cases. In school cases, minorities are supposed to be spread around perfectly evenly among districts; in legislative cases, they are supposed to be segregated as effectively as possible. Whether pie wedges are mandatory and concentric circles prohibited, or the reverse, depends simply on whether the projected activity is voting or schooling.

There is still a chance for the Court to pull back from this abyss. The simplest thing it could do is hold that Congress codified the *White* v. *Regester* intent test in 1982. More ambitiously, it could get the courts and the Justice Department out of the business of gerrymandering entirely. One way to do this would be to hold officials to a standard of color-blindness. If a legislature has enacted a racial gerrymander, one answer is not to impose a judi-mander in the opposite direction, but to construct a scheme which does not take race into account. That is not all that hard to do. Judge John F. Grady, of the Northern District of Illinois, dissenting in another Chicago case, has set out a plausible standard for remedial action:

> The relief I would grant would be a map drawn according to the traditional neutral criteria, without regard to what I believe is the constitutionally impermissible consideration of race or ethnic character. Such a map would consist of compact and contiguous districts, drawn with due regard to the one-person-one-vote requirement as well as natural political boundaries . . . [W]hatever the bloc voting effect of a colorblind map might be, it would be unintended. That, in my view, is the only way the Constitution permits. There is no way to draw racially conscious lines that will be "neutral."

In upholding the constitutionality of the original Voting Rights Act of 1965, the Supreme Court described the practice of racial gerrymandering as unconstitutional. If it still upholds that principle today, it will steer the Voting Rights Act away from the foggy banks of "group choice" and back toward its original purpose of guaranteeing that individuals are free to register and vote as they wish.

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Why the Privatization Movement Failed
Robert H. Nelson
(*Continued from page 26*)

sociation, their members could not afford to buy the lands they use.

In October 1982, the *Idaho Statesman* reported more reaction:

> "If this continues, it could put a lot of ranchers out of business. People don't realize just how serious this is to stockmen," said rancher Louis Cenarrusa, a brother of Idaho Secretary of State Pete Cenarrusa.
>
> Ranchers could not compete with "tourists and out-of-state interests," who pay high prices for land in Blaine County, rancher Bud Simpson said.
>
> Asked what he could do to stop the Reagan administration's program, [Idaho Governor John] Evans said, "We'll call out the National Guard if necessary. We're not going to be bullied on this."

In addition, the privatizers' goal of long-run ideological education turned out to be incompatible with short-run political success in selling land. The market-oriented and libertarian themes offered by the privatizers rallied opponents as well as supporters. To describe the public land estate as a nationalized industry—domestic "socialism"—typically alienates rather than conciliates defenders of the public lands. Public opinion became inflamed and debate polarized to the point that—distrusting the motives of the land agency administrators—an aroused opposition refused to give them the discretionary powers needed to pursue even the modest sales of 4.4 million acres that were the immediate focus of the Interior Department plan. Trapped in a debate over whether to sell millions of acres, Interior managed to lose the ability to sell street-corner lots in Reno and Palm Springs.

The governors of the public land states, who though predominantly Democratic had often found Watt's land policies congenial, began to speak out against the privatization effort. It is interesting to note, incidentally, that western states, while criticizing Interior's privatization efforts, have moved fairly aggressively to sell some of their own lands. Indeed, they have sold much more than the federal government in recent years—192,585 acres from 1972 to 1981, compared with only 67,765 acres for the Bureau of Land Management.

This discontent was of deep concern to the White House. The West had been the bedrock of Reagan support, and his administration had

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come into office pledging to quell sources of western resentment. Hence the days of privatization were numbered.

A New Strategy

The proponents of privatization had always recognized that there might be political problems and they sought to tailor plan details accordingly. The general strategy would be to subdivide the rights to use public lands into an assortment of grazing rights, hunting rights, mineral rights, water rights, and so on, and concede to users the rights to public lands that they already held *de facto*—and in some cases had largely paid for. The government would then sell off any still-unappropriated rights. Steve Hanke, a staff economist for the Council of

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Public Policy Week

AEI's Eighth Annual Public Policy Week will be held December 3–6, 1984, at the Mayflower Hotel, Washington, D.C.

Watch coming issues of *Regulation* for program details. For further information, call 202/862-6432.

Conference sessions will be devoted to economic outlook, international affairs, trade policy, public opinion, elections, community development, health, energy, regulation, religion, education, and the media.

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Economic Advisors, and a key architect of privatization, proposed to give existing ranchers, in effect, grandfather rights by means of an option to purchase outright the permanent grazing rights to their plots at a highly preferential price. This price would be set to equal the expected future value of the public grazing fees they would otherwise have paid. Meanwhile, public access for hunting and other recreational uses would be maintained.

There were several major problems with this strategy. First, explicitly defining the boundaries of the various user rights and allocating them among users was sure to be an administrative nightmare. (The long-standing separation of surface rights and underground coal rights on federal lands has been a major administrative headache for federal coal managers.) The existing de facto user rights are fuzzy, but serviceable; while nobody knows exactly what the actual bounds are, for example, between a rancher's grazing rights and hunters' interest in preserving enough forage to support wildlife, the division works in practice. But political conflicts between different users would be sure to break out if the government tried to define these bounds formally.

Moreover, if all de facto rights to public land were to be recognized, there might be few if any rights left to sell. It may be that the only important public land rights that are not already being used are mineral rights, and to some degree even they are allocated. Many miners believe the current mining law gives them a permanent entitlement to explore on public lands and keep any minerals they discover.

It is also doubtful whether the general public would be willing to concede in principle what it long ago effectively conceded in practice, which is the use of the public lands in question for private rather than national benefit. Rightly or wrongly, the public would probably perceive formal recognition of existing user rights as a "giveaway"—which is precisely the position taken by Joshua Muss, the executive director of the Property Review Board.

The Demise of Privatization

In many ways, the privatization effort resembled the Carter administration's "hit list" of water projects. Both initiatives made sense from a national efficiency perspective, but foundered because they would have upset land management practices of long standing. Both were pushed by policy makers with strong convictions but little practical experience with public land management. Both were more or less foisted on the respective secretaries of the interior, Cecil Andrus and James Watt, who sustained great political damage in defending programs not of their own devising.

The irony is that it was the privatizers who were following the cherished principle that public lands must be used for the broadest public benefit. Reducing the federal deficit and paying off the national debt would be of general national interest. The opponents of privatization, despite much rhetoric about the squandering of the public patrimony, drew considerable political strength from the interest groups that enjoy special benefits from preferential access to public land and influence over public land management.

The irony is that it was the privatizers who were following the cherished principle that public lands must be used for the broadest public benefit.

Momentum is powerful in government, and it was not until the summer of 1983 that the effort to privatize the public lands was officially ended. On July 15, 1983, Secretary Watt announced that he had reached an agreement with Edwin Harper, the chairman of the Property Review Board, to exclude public land sales from the jurisdiction of the board. Watt also pledged in a letter to the western governors that "the mistakes of 1982 are not being, and will not be, repeated. Each governor has been briefed, or his staff has been briefed, on our plans for disposing of the few isolated tracts in the respective States." Watt abolished both Interior's asset management office and the BLM's official liaison with the Property Review Board.

For all the fierceness of the controversy, the privatization effort had little substantive impact. As Table 3 shows, land sales continue at a level of approximately zero. Less land has been sold in the past ten years combined than in any single year from 1950 to 1968. There has

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Table 3

SALES OF PUBLIC LANDS BY THE BUREAU OF LAND MANAGEMENT

Fiscal Year	Parcels	Acres	Receipts
1950	563	65,054	$ 456,259
1955	963	168,013	1,925,975
1960	701	99,225	5,101,297
1965	592	87,061	3,061,158
1968	346	66,632	2,521,132
1969	274	37,877	1,802,126
1970	258	35,150	2,099,849
1971	219	30,113	2,013,823
1972	170	22,005	1,941,520
1973	148	13,669	1,797,933
1974	79	8,691	2,055,637
1975	69	5,105	233,438
1976	84	3,641	584,751
1977	24	1,295	284,964
1978	16	709	82,585
1979	86	1,760	6,480,499
1980	159	4,115	7,326,599
1981	111	7,120	2,868,087
1982	55	1,312	1,466,022
1983	223	10,257	8,172,601

Note: Land sales in Alaska are excluded.
Source: Interior Department data.

been no appreciable progress even on the sale of scattered parcels of urban and range lands: those parcels potentially amount to several million acres, hundreds of times more than was sold last year.

Incremental Privatization

For a year or more, the doings of the Property Review Board made privatization the central issue in public land debates, which were widely covered in the western press. Although this high visibility had the disadvantage of polarizing the issue, it exposed the public to new information and concepts, and in the long term widened the agenda for policy debate.

Students of land tenure have found that new property rights are seldom planned, nor do they proceed in large jumps. Rather, they evolve incrementally in response to the needs and pressures of the moment. Even many instances of "landmark" legislation have simply ratified existing trends and perhaps pushed them along a bit further. The Forest Service, for example, had been creating wilderness areas administratively for forty years before Congress first gave formal statutory recognition to the concept in the Wilderness Act of 1964. The Federal Land Policy and Management Act of 1976 followed a similar pattern.

Mining law on the public lands arose from informal private arrangements worked out in the nineteenth century among western miners, who needed a quick way to resolve potential conflicts in mining claims. Similarly, the Homestead Act of 1862 evolved when the government eventually acquiesced in widespread squatting on public lands. For a long time, settlers had honored informal private arrangements whereby, should the government offer the land for sale, the settler in residence had a right to be the sole bidder and thereby get the land for the minimum price, generally $1.25 an acre. Interlopers could be shot for challenging these arrangements.

Grazing rights on public lands also evolved over many years. Much like the squatters, many ranchers worked out informal arrangements to allocate unappropriated areas of public land among contending users. The Taylor Grazing Act of 1934 allocated public land grazing "privileges" on the basis of ranchers' historic use of the land and ownership of complementary "base property."

Times have changed since the days of the squatters: land users now establish rights to exclude other users from public land by political rather than bodily means. Success has come to depend on political strength, not physical strength—the quick lobbying campaign, not the quick draw. Seen in this light, de facto privatization of the public lands has been occurring throughout this century and has proceeded still further in the past five years.

Times have changed since the days of the squatters: land users now establish rights to exclude other users from public land by political rather than bodily means. Success has come to depend on political strength, not physical strength—the quick lobbying campaign, not the quick draw.

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On much of the public grazing lands, for instance, ranchers have maintained their dominant influence against the recent assaults of environmentalists. Property rights in grazing allotments are still imperfect, since the BLM can set terms and conditions for grazing. But for fifty years now, the bureau has almost never canceled any grazing privileges. And more recently it has been trying to placate rancher interests in various ways and enlist ranchers in land management. For a decade BLM discouraged ranchers from financing their own range improvements; now it has reversed that policy, and has also assigned them much more responsibility for maintaining such investments. In a limited number of cases, ranchers will be given more scope to decide grazing practices themselves under formal "cooperative management agreements." As long as the issue is kept at a low profile, ranchers probably can expect even more incremental expansion of the security of their grazing rights.

Wilderness organizations have shown even more impressive success in controlling "their" chunk of the public land estate. They fended off oil and gas exploration in wilderness areas in a highly publicized battle. Hunters, hikers, fishermen, and other recreationists have also bolstered their collective access rights to public lands in recent years. Incidentally, some supporters of privatization have proposed giving wilderness organizations formal title to federal wilderness areas, thereby recognizing officially that these organizations now in effect already hold a sort of collective property right in wilderness areas.

Another form of privatization has thrived even though it is illegal. According to Forest Service estimates, marijuana growers in California and elsewhere have diverted as much as 1.5 million acres of the national forests to their own use. Law enforcement agencies have been as helpless as their nineteenth century predecessors in driving these squatters off the public lands.

One other recent case of de facto privatization deserves mention. Around half of federal coal lies under private surface lands. As a practical matter it has always been hard to develop this coal against the wishes of the private surface owner. In 1977, in the Surface Mining Control and Reclamation Act, Congress formalized these rights by adopting a requirement that would-be miners obtain the consent of "qualified" surface owners. It is worth noting that this action had the active support of environmental and other groups that normally are strongly opposed to such privatizing measures.

This informal evolution of private rights to public lands has a number of advantages. It provides security to users, and encourages their interests in properly maintaining and managing the land. In both respects, however, it falls short of outright privatization. Perhaps most important, it makes it hard for existing users to transfer the land to new users. Ranchers face numerous restrictions on sales of grazing rights; many other user groups cannot legally sell their de facto rights at all. The rules also make it hard for users of different sorts to negotiate their differences and reach reasonable compromises. For example, as has received considerable attention by now, the Audubon Society allows carefully controlled oil production in its Rainey bird sanctuary in Louisiana. It has every incentive to fight similar drilling in federal sanctuaries, however, because it would suffer all the risks of that drilling but get none of the benefits. If it actually owned the wilderness areas, it could use the large oil and gas royalties to buy more land to expand the overall sanctuary system.

The rights of state governments over federal lands, like the rights of private parties, have been advancing bit by bit as well—accomplishing some of the goals of the Sagebrush Rebellion after all. Western state governments have shown great strength in the debates over deployment of the MX missile and the siting of nuclear waste facilities. Regional "teams" that include representatives of western states have acquired a central decision-making role in the federal coal program; the BLM is seeking to apply this model to other public land decision making as well. The BLM worked out its congressionally mandated plan for the management of the twelve-million-acre California Desert Conservation Area with the extensive involvement of state and local groups.

In recent years the federal government has agreed to try to make its land use plans consistent with state and local plans. A 1972 law requires that federal actions be "consistent" with state plans for the control of coastal zones. There has been a major battle over the meaning of this wording. Western state officials have

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argued that the consistency provisions of the Federal Land Policy and Management Act—which are weaker than those of the coastal legislation—should nevertheless be interpreted with a similar stringency. Some westerners have recently proposed that the actions of federal public managers be required to conform to the decisions of local zoning authorities—just as if the federal government were a private landholder. It is even possible that the states might end up with *more* power over the federal land than if it were privately held.

This might be the most convenient outcome of all for the western states: they make the decisions, while the federal government continues to pay for the administrative apparatus and its management costs. The subsidy, of course, is nothing new; what is new is the further shift of control. It remains to be seen whether this arrangement will prove acceptable to the East and Midwest, which are asked to bear the financial burdens, but to forgo more and more of their already limited prerogatives of owning the land.

But even if the East accepts this arrangement, the western states are likely to find that they cannot manage federal land very well by remote control, by trying to bind the hands of federal land managers in advance with rigid rules and requirements for consultation with the states. Too much discretion is necessary and the transaction costs will prove too large. The logical eventual step is for western policy makers to use their new-found prosperity to accept the costs and responsibilities of management under direct state ownership of the land.

. . . the western states are likely to find that they cannot manage federal land very well by remote control, by trying to bind the hands of federal land managers in advance.

The Long-Run Prospects

Since legislation tends to ratify pre-existing trends in property rights, the best way to predict the long-run future is to observe the incremental trends of the recent past and present. As we have seen, these trends show less federal control over public lands and more private and state-and-local control. In effect, privatization and the Sagebrush Rebellion are actually being implemented, even if slowly and incrementally, and even if the process is obscured by myths and fictions that camouflage its inconsistency with widely accepted political beliefs. In some ways, the public and private land systems seem to be gradually converging, as governments increase their control over the use of private land through zoning and other regulations, and as private rights proliferate on public lands.

The speed at which such a new system of public land tenure can evolve depends on several factors. Probably the most important is ideology. These evolving processes have not been recognized formally in part because most Americans are still not convinced they are a good idea. Yet the premises of the current public land system are no longer believed either. The public has lost most of its confidence in the notion, dating back to the conservationist ideology of the turn of the century, that resources can be handed over to objective, "scientific" management by experts. Most leading political scientists have given up on the idea that there is a single identifiable public interest, and instead see a multiplicity of competing and conflicting interests—the perpetual conflict among whom does not necessarily produce anything much resembling a public interest. In short, public land institutions now rest on an intellectual foundation that is much eroded.

If significant changes in public land tenure are to occur, they will probably require combining a popular movement such as the Sagebrush Rebellion with an intellectual base such as that of the privatization movement. Almost for the first time in this century, there are now effective academic and other intellectual proponents of major changes in public land tenure —although, of course, professional opposition to their views is also strong. Until their ideas can be translated into an acceptable popular ideology, however, they will have little chance of full success. The outcome of their efforts will help determine whether historians see the Sagebrush Rebellion and the privatization movement as a footnote to the stormy history of the West or as the beginning of a remarkable new chapter. ■

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Readings
of particular interest

The Specter of Medical Rationing

The Painful Prescription: Rationing Health Care by Henry J. Aaron and William B. Schwartz (Brookings, 1984), 161 pp.

Health care costs continue to climb rapidly in the United States. By contrast, Great Britain spends barely half as much per capita on hospital care as does the United States. What has Britain sacrificed in exchange for cost control, and will the United States have to make similar sacrifices if it is to cut costs? Henry Aaron, a senior fellow in the Brookings Economic Studies Program, and William B. Schwartz, M.D., Vannevar Bush Professor at Tufts University Medical School, address that question here.

The British health care system, unlike ours, is largely nationalized, and most physicians are salaried employees of the government. The government allocates a specific portion of its budget to the National Health Service and all hospitals must limit operating expenditures on NHS patients to the fixed sum they receive, which sharply limits the resources spent on medical care. To find out how this limitation affected medical practice in Britain, Aaron and Schwartz compared the use of several medical procedures in the two countries.

They found that Britain reduces costs not by lowering the quality of services, in most instances, but by limiting the quantity of services provided. For example, Britain uses CT scanners that are similar to those in this country, but has only one-sixth as many of them per capita. Likewise, Britain performs half as many x-ray exams and one-tenth the amount of coronary artery surgery per capita as we do. British doctors treat acute, life-threatening illnesses as aggressively as Americans in younger patients but not, in some cases, in the elderly.

The proportion of the British population on hemodialysis, a long-term and costly treatment necessary for the survival of patients with kidney failure, is one-third that of the United States. In Britain the procedure is rationed primarily by age. Up through age 44, British dialysis rates are the same as France, West Germany, and Italy; for ages 45-54 the rate is two-thirds that of those countries; for ages 55-64 it is one-third; and for ages 65 and over it is less than one-tenth. In addition, patients with physical handicaps, mental illness, diabetes, and hepatitis are less likely to be treated than are other patients.

These criteria are not explicit, yet rarely do "unsuitable" patients present themselves at a dialysis center. This is because general practitioners and internists screen potential patients and do not refer "unsuitable" patients for treatment. Both sides thus avoid facing the psychological implications of the official decision to deny care. Many British doctors seem to feel, however, that even if resources were unlimited they would not recommend dialysis for many of the sorts of patients who are treated in the United States.

Several other factors in addition to age seem to influence British resource allocation. One is geography. The National Health Service inherited wide regional variations in per capita spending; with little growth in the NHS budget, poorly served localities have had a hard time catching up because they can gain only at the expense of another. Another factor is the emotional and psychological anxiety aroused by a disease such as cancer. Radiation therapy is available to all who can benefit from it. Metastatic tumors responsive to chemotherapy are always treated, although nonresponsive ones frequently are not.

Aaron and Schwartz also observed that the British treat highly visible unusual illnesses intensively. Hemophilia, an uncommon disease whose symptoms alarm any observer, is treated at the same rate and almost as intensively as in the United States. By comparison, the severe pain and diminished endurance caused by an-

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gina are less visible social problems, and coronary artery surgery to correct angina is performed only a tenth as often in Britain as here. In addition, patients who must do without coronary artery surgery can usually still hold a job, although many must make major adjustments in life style.

Surgery or therapy is more commonly provided in Britain in cases where withholding it is likely to leave the patient as a burden on society. Medical service is also more likely to be provided if the aggregate cost of treating all cases of a given type is relatively low.

Rationing decisions generally fall hardest on capital-intensive procedures. The NHS tightly controls capital expenditures on CT scanners and other expensive equipment but finds it difficult to monitor expenditures that show up as higher hospital operating expenses. As a result, British spending on "total parenteral nutrition" (a form of intravenous feeding), is high relative to spending on CT scanners: reallocating money from the former to the latter could provide more benefit to the average patient. However, both services are undersupplied by U.S. standards: Britain spends only one-quarter as much per capita on TPN as does the United States.

British patients awaiting hip surgery must wait many painful months or even years for treatment. There is a way, however, for such patients to "jump the queue" and receive immediate treatment. Private hospitals and clinics have been growing rapidly, and now perform up to 25 percent of the hip replacements in some parts of Britain. NHS physicians are allowed to spend part of their time treating private patients, either in the 2,800 "pay beds" in NHS hospitals to which private patients can be admitted or in the growing network of wholly private hospitals and nursing homes.

Aaron and Schwartz contend that the savings that can be realized from eliminating wasteful procedures are not going to be enough to control health costs in the United States. At some point benefits will have to be forgone. But several obstacles hinder the adoption of British-style cost-cutting moves here, aside from the incentive our payment system gives physicians and patients to maximize medical treatment. Americans are more accustomed than Britons to receiving a very high level of care, more knowledgeable about medical advances and treatments, and more likely to challenge a physician's diagnosis and therapy. And special interest groups can more easily form to lobby for particular groups of patients in the United States.

Consult before Digging

Facility Siting and Public Opposition by Michael O'Hare, Lawrence Bacow, and Debra Sanderson (New York, 1983: Van Nostrand Reinhold), 223 pp.

There are many important facilities that most people believe should exist, but that hardly anyone wants to have as a neighbor. Such facilities are diverse, ranging from freeways and airports to halfway houses and prisons to power plants and hazardous waste depositories. In the past two decades mounting political opposition on the local level has made it increasingly difficult, in some cases impossible, to find sites for such facilities.

The political difficulties of siting cause a number of serious problems, according to the authors of this book (O'Hare is a lecturer at Harvard's Kennedy School of Government, Bacow is associate professor at MIT, and Sanderson, president of CLTW, a consulting firm, was assistant secretary of environmental affairs for the state of Massachusetts). Some projects never get built at all. Despite thirteen unsuccessful attempts to build oil refineries in New England in recent years, the region must still import its refined oil from outside. When new construction becomes impossible, society goes on relying on older facilities that are overcrowded, outdated, and ironically often noisier or dirtier than the new would have been. Even when a needed facility is built, political snags drive up its price, encouraging it to be built in the wrong place, and taint its later relationship with the host community.

The authors criticize the traditional method of making siting decisions—what has been called the "decide-announce-defend" pattern. In that pattern, a developer first chooses what to build and where to put it on technical grounds, consulting with engineers, market analysts, lawyers, and perhaps local government officials. It may then—if it is a private company—assemble the necessary land quietly

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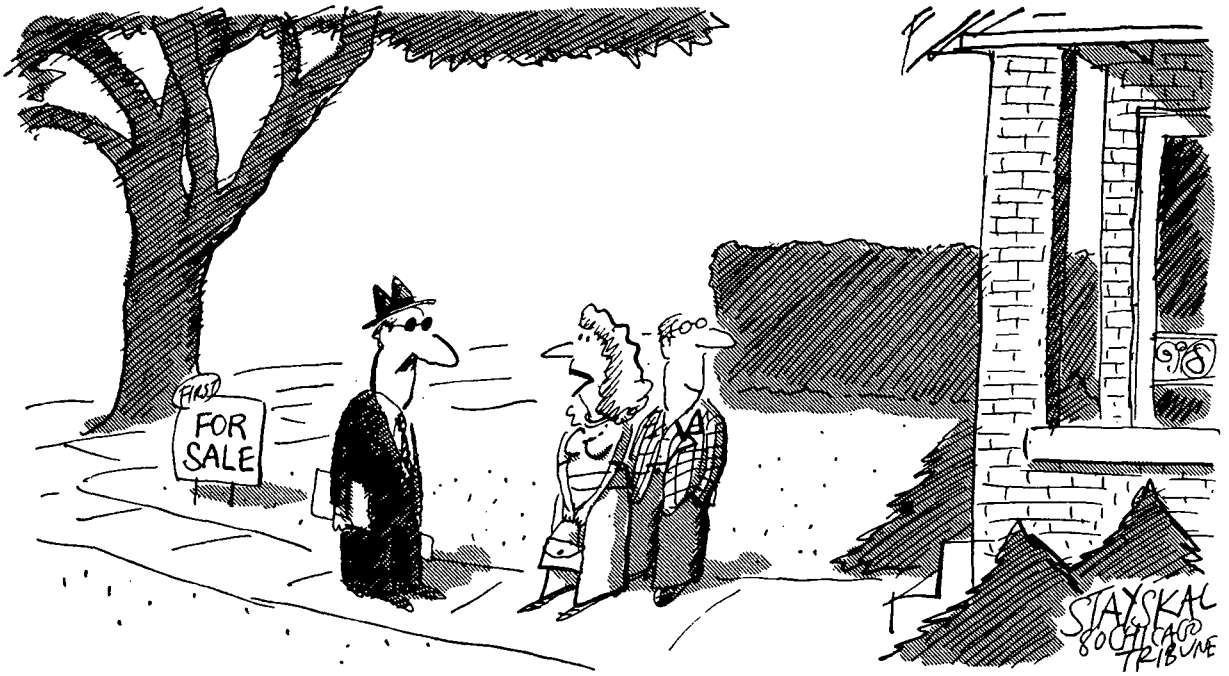
so as to avoid driving up its price. Neighbors may first learn about the project in a local paper, when the bulldozers are already around the corner. When an opposition begins to mobilize—its urgency spurred by the fear that the project will soon be a *fait accompli*—the developer may be genuinely surprised, having expected that its negotiations with local government officials had settled such questions.

The logical course for opponents at this late stage is to block any permits the developer has to apply for. Although lawmakers have often assumed that increasing public participation in the permit process will help iron out differences, the authors say, it really encourages polarization—especially when advocates are using a public hearing to build a record for judicial review. Furthermore, "people have better things to do than commit large amounts of time to the business of government."

Developers often falsely imagine that neighbors will go along once they are told why the site is technically the best place for the project. Failing that, they imagine that making it through the hearing process will guarantee them the right to build. But the opponents have several bites at the apple: if they cannot stop the granting of permits or prevail in court, they can interest other regulators in the matter—at local, state, and federal levels. Finally, or simultaneously, they can turn to media campaigns, political pressure, or disruptive demonstrations.

The authors believe that it is often impossible to defeat such local opposition; the better course for developers is to defuse it by compensating the neighbors of a facility. Negotiated compensation encourages both sides to suggest design or site changes that could render the project less obnoxious to the neighborhood. There is also a case for compensation on grounds of straight efficiency, since it makes the developer take into account the social costs of its project.

But the authors warn that outright monetary compensation may not work in all cases. Sometimes a conditional form of compensation is best. The developer may offer, for example, to make good any future losses in neighbors' property values. Contributions to particular public services put under strain by the facility are also a good way to placate opposition. If the project will inflict damage on, say, recreational values, the developer can contribute services in kind, as by dedicating a nearby parcel to recreational use.



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"We like this one . . . How far away is the school, train station, church, grocery store and nuclear power plant?"

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Compensation of any sort works best when it is directed at near neighbors and at those whose objections to a facility are based on tangible impacts rather than ideological considerations. Moreover, the community must be well enough informed to get an idea of the risk it is being compensated for. Thus, the authors say, negotiated settlement demands a flow of timely information to the affected parties. Developers should consider paying initial grants of money to the neighbors to help them inform themselves, since the manner in which the information is provided affects the candor, completeness, and objectivity with which it will be credited.

Some of these recommendations have already been applied in practice. A 1980 Massachusetts law, discussed extensively in the book, provides for local government participation in a negotiated compensation process before hazardous waste processing facilities are built.

Preservation, Paralysis, and Policy

"Landmarks Preservation in New York" by Joseph B. Rose, in *Public Interest*, no. 74 (Winter 1984), pp. 132-145.

Twenty-five years ago many urban reformers believed that the solution to the problems of the big cities was to tear down obsolete buildings and replace them with modern, ordered, and pristine towers. Today, reformers are keen on preserving architectural history and heap praise on such projects as the renovation of Boston's Faneuil Hall and New York City's South Street Seaport. The focus of city-planning activism has swung from compelling the demolition of old buildings to prohibiting it.

Influenced by the movement for historic preservation, many cities have passed laws that prohibit owners from tearing down or redeveloping buildings that have been designated by a city panel as landmarks. In this article, Harvard doctoral candidate Joseph B. Rose discusses charges that mandatory preservation has "run amok" in New York City, endangering both the economic vitality of the city and the property rights of its residents.

In 1965 New York City passed a pioneering law creating an eleven-member Landmark Preservation Commission (LPC) with the power to designate individual landmarks and historic districts and regulate their use. Structures so designated must be kept in "good repair" and cannot be demolished or altered in any way without the permission of the LPC. Failure to abide by these restrictions is punishable in some cases by imprisonment.

At first the LPC was circumspect in its decisions to designate privately owned structures, Rose says. Its perspective changed, however, following the Supreme Court's 1978 ruling in *Penn Central* v. *City of New York*. In that case the Court rejected a contention that it was unconstitutional taking of private property rights without compensation for the commission to prohibit the construction of an office tower above Grand Central Terminal. Instead, it ruled, the action was a constitutional exercise of New York City's "police power," much like a zoning ordinance.

Soon the commission began to expand its original limited purpose. Under attack for preserving only the "elite" portion of the architectural past, the commission began assigning landmark status to buildings and districts that cast light on "social history" by showing how the average person lived. What had begun as an effort to preserve "the history of the very famous and the wealthy" became a crusade to "record the history of the ordinary," in the words of one commission member. "This coupling of historic preservation with democratic social history has made it difficult to disqualify *any* aged structure," the author says. The commission has to date designated more than 16,000 buildings, many of whose owners objected to landmark status, along with such features of the urban scene as an old elevated subway track (characterized by the City Planning Commission as a blight) and the gnarled street plan of lower Manhattan.

"One explanation for the LPC's aggressive behavior," Rose says, "is the relative ease with which it implements its administrative decisions." The City Planning Commission has official authority over neighborhood planning and zoning matters, but its decisions to restrict development are easily overturned by the city's Board of Estimate. In the wake of the *Penn Central* case, the city gave the LPC sweeping emergency powers inhibited by virtually no such checks or balances. As anti-development

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activists turned to landmark designations to block an ever-growing number of projects, Rose claims, the commission began to usurp many of the CPC's statutory responsibilities. Churches and theaters of "dubious aesthetic significance" became a favorite target for landmarking, Rose says, in part because of a predilection for buildings of low height. He quotes the *New York Times* architecture critic, who wrote: "One of the greatest gifts the city's churches and theaters convey . . . is the open air above them." Whatever its virtues, however, open air is hardly (in the author's view) the sort of "architectural landmark" the LPC was enacted to preserve.

Although there is an appeals process and a "hardship clause" exception to LPC rulings, Rose says that in practice neither one is much of a curb on the LPC's power: "of the more than 16,000 designated landmarks in New York City, only five owners have ever been granted permission to demolish a building due to reasons of economic hardship." The owner of a building can appeal a landmark designation only after it takes effect. The appeal process can stretch on for years, which is deadly to prospective developers who must pay interest charges on the unused land.

Because it fails to compensate property owners for the costs it imposes on them, the LPC is free to tread casually on private property rights, says Rose. He adds that it impairs the city's tax base by discouraging new development and lowering the value of existing real estate. (The commission explicitly ignores such financial considerations in its designation process.) If the LPC had to take into account the costs of its decisions, it would act with more restraint.

Although the economic costs of preservation do "not necessarily . . . make all designations inappropriate," Rose says, fairness dictates that the costs not be loaded onto the shoulders of a small number of owners. Since direct compensation would be expensive and politically unrealistic, Rose proposes alternative ways to do so at no cost to city treasuries. One costly effect of landmark designation typically is to make owners forgo much of the height and density that the zoning laws would permit on the site. A way to compensate owners for landmarking is to allow them to sell these unusable height and density rights to other landowners, who would then be permitted to add more stories to their buildings elsewhere. Such a scheme, Rose believes, would strike a better balance between the aims of preservation, the property rights of citizens, and the well-being of the city.

A Skeptical Look at the Ministry of Aesthetics

The Democratic Muse: Visual Arts and the Public Interest by Edward C. Banfield (Basic Books, Inc., 1984), 244 pp.

The federal government has long subsidized the arts by means of land grants, tax exemptions and deductions, and the like. It briefly ventured into direct funding, also, between the Depression and World War II, when the Section of Fine Arts in the Treasury Department and the Works Progress Administration provided relief to thousands of unemployed artists. Still, the creation in 1965 of the National Endowment for the Humanities and the National Endowment for the Arts was a watershed. It legitimated the idea of a "national cultural policy" and cemented the bond between art and the federal government as no previous act of Congress had done.

In this book, Edward C. Banfield, George D. Markham professor of government at Harvard, reviews the record of the NEA principally (though not exclusively) in connection with the visual arts. In addition, he examines two other channels of federal subsidies, direct and indirect, to the visual arts—to art museums (of which there are presently around 200 that have operating budgets of $250,000 or more) and to art education in the public school system. These institutions, he argues, have tended to provide the public with experiences incidental to the aesthetic: art as entertainment, antiquarianism, therapy, and so on. Yet if there were any justification for public funding of art institutions, he believes, it would be to promote aesthetic experience in the public.

Banfield suggests that NEA, not unlike many other federal agencies, has tried to further its own growth by building constituencies, even going so far as to subsidize publications advising museums how to influence federal leg-

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islation. In turn, the endowment has served to enhance the images of incumbent politicians as supporters of the arts. (Richard Nixon in 1969 asked Congress to double the appropriations for both endowments on the advice that it was a "quintessentially presidential thing to do.")

NEA officials have kept a good deal of relative liberty in the awarding of grants. Their tendency to favor avant-garde and radical art has led them to fund projects, especially grants made to individual artists, that some outraged members of Congress have characterized as bizarre. In 1974, acting chairman Michael Straight refused to approve a set of grants whose stated purposes he deemed frivolous. The endowment responded by changing its rules: "hereafter, applicants were not to say what they intended to do with the fellowship."

The typical art museum, like NEA, pursues a goal of self-preservation—which in its case means trying to enhance the prestige and size of its collection in order to attract support. Prestige is obtained by acquiring recognized masterworks, but because all or most of the museums that bid for such works are subsidized, prices are driven up to staggering levels (and then serve in turn to justify higher subsidies). The major museums acquire far more objects than they can display. This means that many valuable works are never or seldom exhibited and that the storage itself, often in spaces that occupy valuable downtown property originally donated by the government, is an expensive proposition. When expansion becomes necessary, government must again bear the cost: "it has been estimated," Banfield writes, "that state and local governments have provided 40 percent of the cost of museum buildings."

In trying to justify their status as public institutions, museums have had to emphasize their role as "educators." In these and various other "outreach" programs, according to Banfield, aesthetic concerns became subjugated to social ones. Another ploy is to organize costly "blockbuster" exhibits that draw crowds so large that each patron is often limited to a few seconds of viewing. (NEH helped underwrite the cost of nearly all such exhibits from 1972 to 1976, and NEA, by the end of fiscal 1980, had given museums $100 million in matching grants for crowd-attracting activities.) Not only are such exhibits expensive—shipping around objects from city to city is costly (and bad for the objects)—but they also force museums to devote more of their resources to public relations at the expense of maintaining their own collections.

Art education in the public school system dates back to about the same time as the founding of the large museums and had the same original purpose: moral education. Only in the last twenty years, however, has the federal government become heavily involved. The Elementary and Secondary School Act of 1965 provided $150 million for developing new curricula, fostering new approaches to teaching art, and so forth. According to Banfield, most of the money went for "isolated performances and one-day 'cultural trips' [which were] sharply reduced in 1970, when an evaluation showed that these activities had little lasting educational value." The NEA, for its part, began an "Artists-in-Schools" program, which has been criticized as little more than a way to find employment for artists. The National Art Education Association reported in 1977 that the federal government had, despite many efforts, had "little impact" on traditional art education. Indeed, the programs' major effect seems to have been to stimulate the growth of an active lobby of art educators.

Banfield's view is that—given the premises of the American political tradition—visual art is not within the proper sphere of the federal government. Private funding of the arts, for all its failings, at least has the benefit of not enabling coalitions to force their chosen extra-aesthetic values on the public. But, given the likelihood that art and government will remain linked for the time being, Banfield offers what he calls two "plausible alternatives" for art policy, in both of which he sees some merit but neither of which he believes would find favor in today's political climate. First, museums should commission reproductions, as close to perfect as possible, of high-quality art. Although devoid of prestige or antiquarian interest, these works would make the aesthetic experience of good art available to far more people than it is now, at far lower cost. "From the public standpoint, it makes more sense to use tax dollars to *increase* the supply and *decrease* the price of art," Banfield says. Second, Banfield proposes that the gap between "fine" and "applied" art be narrowed by emphasizing the

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aesthetic enhancement of objects of ordinary use—thus integrating art into the conduct of everyday life.

More fundamentally, Banfield questions whether the national government should involve itself with the visual arts at all. Some things give pleasure to individual citizens but do not involve a genuinely public interest; others affect the quality of the whole society but are still not the concern of government, either because it cannot manage them well or because government exists for other purposes. "The American regime rests on the principle that the functions of government are to protect the individual in the exercise of certain inalienable rights and to establish the preconditions for the development of competent citizenry."

Tax Law as a Policy Vehicle: Unsafe at Any Speed?

"Bob Jones University v. United States: Public Policy in Search of Tax Policy" by Paul B. Stephan III, in *Supreme Court Review*, 1983, pp. 33-82.

Although the question whether racially discriminatory schools are eligible for tax exemption has been hotly controversial, the Supreme Court's resolution of the issue last year rested on a narrow and technical basis. But the decision in *Bob Jones University* v. *United States* nonetheless raises a significant policy question, according to Paul B. Stephan III, associate professor at the University of Virginia School of Law. The reason is that the decision apparently revives the long-dormant "public policy" doctrine. This doctrine—which Congress had appeared to put to rest in 1969—once gave courts and the Treasury wide discretion to withhold deductions or other tax advantages from taxpayers who, although otherwise eligible for the advantage, had violated some norm of public policy.

The courts and tax agencies had encountered numerous problems in their attempts to elucidate the doctrine before 1969. First was a problem of selectivity: which public policies, of the many possibilities, should implicitly modify tax rules? Tax administrators would seem to have no special competence in making this sensitive political decision. Second, which tax rules should be modified? Third, how can the tax penalty be made proportional to the gravity of the particular offense?

The proportionality question raised perhaps the greatest difficulties. Since the value of a tax advantage depends largely on a taxpayer's bracket and overall tax situation, denial of the benefit leads to an essentially arbitrary distribution of punishments that cannot be justified on grounds of either deterrence or moral desert.

Perhaps because of frustration with these problems, Congress in 1969 added provisions to the Internal Revenue Code that indicated strong disfavor for the doctrine. Since then, the author says, "the principle that Congress alone should convert income-measuring rules into sanctions for misbehavior has generally prevailed."

Until the *Bob Jones* case, that is. Stephan says the Court looked hard for some way to outlaw racial discrimination in tax-exempt private schools without having to revive the public policy doctrine. But its effort failed. Neither the historical law of charitable trusts, nor the Treasury's traditional treatment of charitable exemptions, nor the actions of Congress on the issue, provides a satisfactory distinct basis for denying Bob Jones University its exemption.

It is often argued that exempting charities and charitable deductions from taxes is a striking departure from a general pattern of taxing economic transactions, and is justifiable only as an attempt to accomplish public purposes. Accordingly, the argument runs, the exemption ought to cover only those charitable donations and institutions that truly serve public purposes by, among other things, complying with public policy. Stephan outlines a different rationale for the charitable exemption. Taxpayers are allowed to deduct donations from their taxable income simply as a matter of defining their *net* income; the money they give away to others is naturally not treated as if they had kept or spent it. Charities themselves are not subject to business taxes because they do not seek profits. Thus the charitable tax provisions, far from being a special privilege calling for a quid pro quo, are fully consistent with the effort to tax net income and business profits.

By denying the exemption, the Court reopens all the problems it previously encountered with the public policy doctrine. The In-

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ternal Revenue Service must now attempt to determine, first, what constitutes racial discrimination, and second, what institutions besides schools and what evils besides racial discrimination should fall within the scope of the public policy rule. Further, the service must decide what are the ripple effects of an exemption denial: do students lose the tax exclusion of their scholarships, faculty the exclusion of their fellowships, and parents the exemption for student dependents? And how should the service measure the taxable "income" of a school that does not pursue profit? Stephan warns that the sanction may result in disastrous consequences for heavily endowed schools guilty of minor acts of discrimination, but impose few costs on hard-core segregated schools that rely for support principally on tuition rather than donations.

There is nothing sacred about tax law, the author says, and no intrinsic reason why revenue collection should be the only purpose that taxation serves. But in a society where an ever-growing public sector requires ever-increasing taxation for its support, the scope of a public policy rule can only become wider and wider, in both range of application and devastating impact on targets.

> *Bob Jones* reflects a simplistic belief that the government, when confronted with something bad (whether illegal or immoral is unimportant), must attack the offending act with every resource at its disposal. The conviction that withholding any potential means of attacking a problem demonstrates a lack of commitment to its solution suffers from two flaws. First, it ignores the possibility that some agencies of government may have comparative advantages as prosecutors of particular policy violations. Second, it ignores the fact that the failure to mold a penalty system to match the policy it enforces has both moral and welfare costs. *Bob Jones* illustrates each of these flaws.

Thus, if only implicitly for the time being, the Court's opinion invites the Treasury and the courts to develop a public policy overlay for every tax rule whose role in defining the base of taxation is not immediately apparent. This, Stephan says, is what makes the case important and the outcome regrettable.

Property Rights in Orbit
(*Continued from page 18*)

quickly and recouped sizable benefits when the Environmental Protection Agency adopted its bubble, offset, and emissions banking programs. Once restraints on arc were lifted, it is a safe bet that a healthy market would soon emerge.

The transition might be more politically acceptable if, like radio and television broadcasters, satellite firms continued to receive their slots free of charge, but could sell them after that. This would, of course, confer substantial rents on the firms that get free slots—rents that would accrue to the public if the government were to claim ownership of the arc sectors allocated to it through the ITU. One solution to this problem would be to require every firm to buy its slot whenever it replaced its existing satellite. This method would also soften somewhat the financial shock to incumbent slot holders who would incur huge unexpected costs if they suddenly had to compete in an auction for the slots they were already using. And since the life of a typical satellite is about seven years, the transition to a market system would not take long to complete.

Another fear might be that firms or consortia might succeed in monopolizing slots (just as some have worried that marketable air pollution permits could be "cornered" in particular regions). As an aside, note that this problem is not unique to market processes—for FCC decisions have themselves tended to distribute more new slots to incumbents than to newcomers. Under a market scheme, judicious application of antitrust laws should be sufficient to guard against undue market power in the arc. Ultimately, of course, the threat of monopoly will be curbed by the increasing competitiveness of alternative technologies, such as fiber optics and terrestrial microwave.

Finally, there is the argument that pricing the arc will make telecommunications services more costly. This is not necessarily so. Much of the current demand for slots is no doubt due to their zero price—that is, there may be fewer serious bidders once they must put their money where their applications are. In addition, pricing the arc might call forth the kinds of technical innovations that have resulted in constantly falling prices for hand calculators, per-

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sonal computers, and a host of other products or services. And if—once a market is working—prices *do* increase, they will be reflecting the true social costs of telecommunications services.

Pie à la Monde?

FCC allocation, as mentioned earlier, is only a final level in the overall administration of the worldwide arc. If a strong case exists for marketing the geostationary arc to U.S. users, perhaps there is an equally strong case for marketing it to international users.

To be sure, persuading the United Nations' ITU to adopt or allow a market approach would be no easy matter. For one thing, some equatorial nations have long argued that if the arc belongs to anyone, it belongs to them by virtue of their locations. More fundamentally, the Outer Space Treaty of 1967, drafted under the auspices of the ITU, implies that the geostationary arc is not really private property at all and cannot "belong" to a nation, much less to a firm: it is another of that growing collection of places and things claimed as "the province of all mankind." In recent years, the multilateral negotiations over the arc have become increasingly politicized along the rancorous lines of the Law of the Sea discussions. There is an important difference between the seas and the arc, however, that augurs well for a global arc market. Although ocean resources (in theory) are not renewable, the geostationary orbit is forever pristine. It cannot be depleted or degraded by the use of satellites. Once their lifetimes end, they can simply be boosted out of the arc.

Next summer in Geneva the ITU will convene the Space World Administrative Radio Conference to allocate additional degrees of arc among competing nations. Suppose the ITU were persuaded to make its initial allocation of the arc to all member countries via political negotiations, as intended, but then to make the resulting slots rentable (though inalienable). This should meet the demand of equatorial and less developed countries that they start on an equal political footing with the technologically advanced nations and that their national rights not be "sold away" (even by themselves). And with a market in arc rental permitted, a less-developed country would be able to lease its slot to any country or firm having the technology to use it, perhaps for the seven or so years that the satellite would be functional. Lessor nations could then, if they wished, use the rental income to develop their own telecommunications network, and could later occupy their slots with their own (or purchased) satellites. Alternatively, they could continue to lease out arc space so long as it was economically advantageous to them to do so.

In our view, organizing such an international market is far preferable to recent proposals that the United States tilt its system of sugar import quotas toward certain equatorial countries in exchange for arc access. The economic advantages of the market alternative are self-evident (who can calculate how sweet the arc is? why further distort agricultural markets?).

Recently the United States has been eager to promote the virtues of competitive markets, especially to nonaligned and developing countries. The FCC now has a golden opportunity to foster the spirit of deregulation both at home and abroad. Surely the commission would like to settle its policy on arc disposal before next summer's international conference, if only to arm our delegation with proof that we are willing to abide by our own principles. Indeed, a U.S. domestic market for arc would have substantial demonstration value to the ITU and just might help pave the way for a global experiment along the same lines. If actions speak louder than words, some FCC action on the arc would well serve pie *à la monde.* ■

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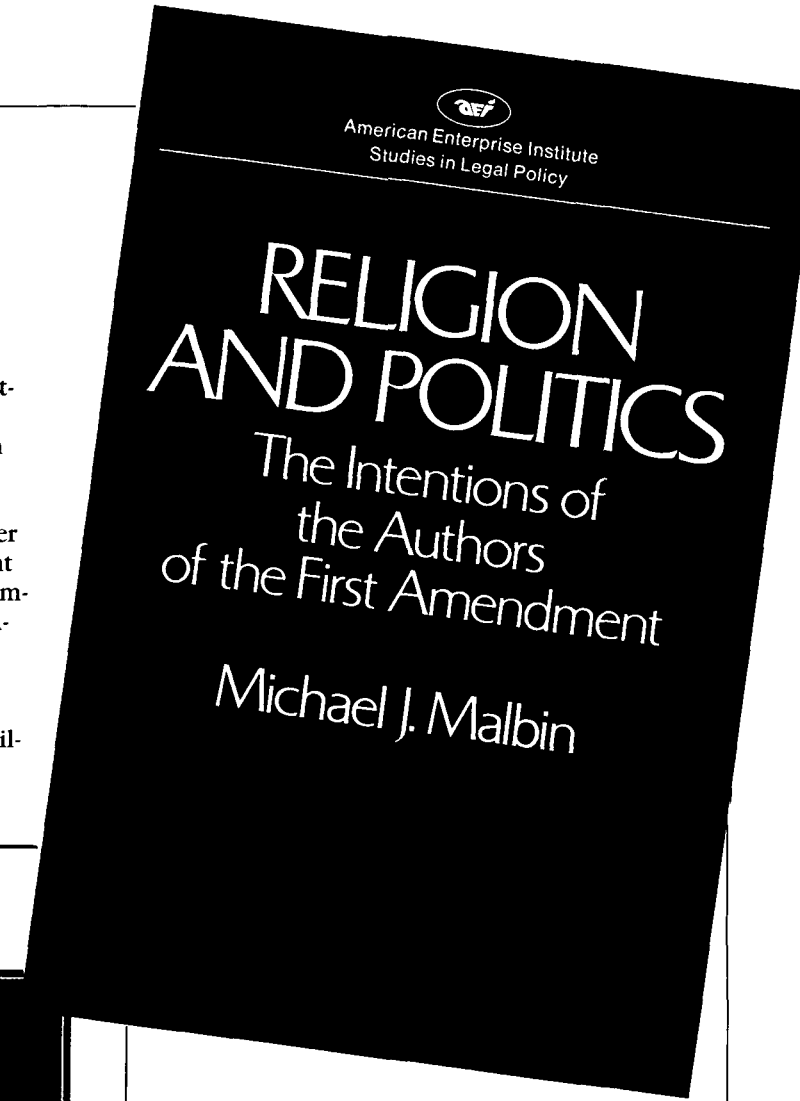
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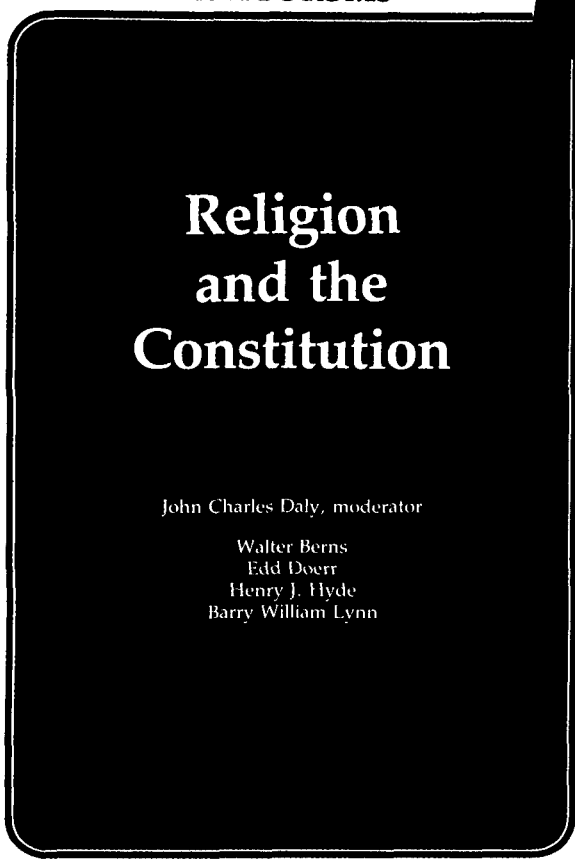

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